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No. 06-525

In The
# Supreme Court of the United States

ANDREA D. WILKES, DAVID H. EHRENWERTH, AND CHARLES R. CLARK, AS TRUSTEES OF THE MARK E. AND MYRNA L. MASON IRREVOCABLE TRUST, MARK E. MASON, AND MYRNA L. MASON,

*Petitioners,*

v.

PHOENIX HOME LIFE MUTUAL INSURANCE COMPANY,

*Respondent.*

**On Petition For A Writ Of Certiorari To The Supreme Court Of Pennsylvania**

## PETITION FOR A WRIT OF CERTIORARI

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## QUESTIONS PRESENTED

In *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985), the Court held that under the Due Process Clause of the Fourteenth Amendment to the United States Constitution, a class action seeking money damages on behalf of the class could bind out-of-state members only if the members received notice that was "the best practicable, 'reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections.'" *Id.* at 812 (citations omitted).

1. If a class-action settlement notice alerts class members to some potential claims against the settling defendant, but withholds material information about other, more substantial, claims known to the settling defendant but unknown to the class members, is the notice sufficient to bind the class members to a release of all their claims?

2. Is the adequacy of the settlement notice determined only by the terms of the formal written notice, without regard to contemporaneous communications made to the recipient by the party providing the notice?

## PARTIES TO THE PROCEEDING

All parties before the Supreme Court of Pennsylvania are named in the caption. In addition to the parties named in the caption, Balanced Equities, Inc., was named as a defendant below but was not served with a complaint and was not a party before the Supreme Court of Pennsylvania.

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## PETITION FOR WRIT OF CERTIORARI

Petitioners, Andrea D. Wilkes, David H. Ehrenwerth, and Charles K. Clark, as Trustees of the Mark E. and Myrna L. Mason Irrevocable Trust, and Mark E. Mason and Myrna L. Mason, respectfully petition for a writ of certiorari to review the judgment of the Supreme Court of Pennsylvania entered July 18, 2006.

## OPINIONS AND ORDERS BELOW

The opinion and order of the Supreme Court of Pennsylvania, including the concurring and dissenting opinions, is not yet officially reported, and is unofficially reported at 902 A.2d 366 (Pa. 2006), and is reprinted in the appendix ("App.") at pages App. 1 through App. 70. The opinion and order of the Superior Court of Pennsylvania is reported at 851 A.2d 204 (Pa. Super. Ct. 2004), and is reprinted at pages App. 71 to App. 89. The opinion of the Court of Common Pleas of Allegheny County is unreported and is reprinted at pages App. 90 to App. 100. The Order of Court and Memorandum in Support of Order of the Court of Common Pleas are unreported and are reprinted at pages App. 101 to App. 104.

## JURISDICTION

The judgment of the Supreme Court of Pennsylvania was entered on July 18, 2006. (App. 41). This Court has jurisdiction under 28 U.S.C. § 1257(a) (2000).

## CONSTITUTIONAL PROVISION INVOLVED

Section One of the Fourteenth Amendment to the United States Constitution provides, in pertinent part, "[N]or shall any State deprive any person of life, liberty, or property, without due process of law. . . ."

## STATEMENT OF THE CASE

Petitioners Wilkes, Ehrenwerth, and Clark are trustees ("Trustees") of a trust created by Petitioners Mr. and Mrs. Mason. For estate planning purposes, the Trustees purchased from Respondent (hereinafter "Phoenix") a policy insuring the lives of the Masons. When the Trustees and the Masons learned that Phoenix and its agent had been providing them with projections that gravely understated the likely future premiums on the policy, the Trustees and the Masons sued Phoenix in Pennsylvania state court.

Phoenix moved for summary judgment on the ground that the Trustees and the Masons were bound by a class-action settlement in New York state court covering hundreds of thousands of policyholders. The Trustees and the Masons replied that the notice in the New York case had been constitutionally inadequate to bind them under this Court's Due Process precedents because (i) Phoenix and its agent had misled them about the effect of the class action on their type of policy, and (ii) the notice referred only to claims that Phoenix had used deceptive general sales practices relating to the nature of life insurance and the reliability of policy dividends, and not to claims that Phoenix had given misleading premium projections to the

Trustees and the Masons and thousands of class members with policies similar to their policy.

**The Policy**

In 1989, the Trustees purchased a form of insurance on the lives of Mr. and Mrs. Mason, known generally as "second-to-die," and, under the label used by Phoenix, "Survivorship Life Protector" ("SLP"). The policy was actually two policies: a whole-life policy with a fixed premium, joined with a term policy with an annual premium that would increase as the insureds became older (called "Optionterm"). The expectation was that if the Trustees and the Masons used the expected dividends on the whole-life portion to buy more whole-life coverage, the amount of Optionterm needed each year would gradually diminish and end. The combined policy operated as a "vanishing premium" policy, so-called because it was intended that dividends on the whole-life part of the policy would in time suffice to offset the premiums owed on the combined policy, so that at some point the Trustees and the Masons would no longer have to make further cash payments to satisfy the premium and keep the coverage in place.

When Phoenix prepared tailored policy illustrations for its SLP with Optionterm, it used the unrealistic assumption that both insureds would live until the younger reached age one hundred. This "no-death" scenario led to lower projected annual premiums than would exist under a more realistic "one-alive" scenario, such as where one of the Masons died at a typical life expectancy and the other survived for several years. In that more realistic scenario, where the death-benefit becomes likely to be paid much

sooner, the premiums on the Optionterm policy would increase greatly; in the present case, by hundreds of thousands of dollars per year. Phoenix knew of the vast difference in effect under the two scenarios, but did not require its agents to disclose the one-alive scenario.

Beginning in 1994, economic conditions caused Phoenix to reduce its dividend payments, which meant that the out-of-pocket payments that the Trustees and the Masons needed to make on the overall policy did not begin to decline as initially projected. The Trustees and Phoenix (sometimes through its agent) discussed the reasons for the changes, and the Trustees and the Masons were given various projections showing how changes in the dividend performance might affect how much the Trustees and the Masons might have to pay over the life of the policies. Unknown to the Trustees and the Masons, all of those projections continued to assume the no-death scenario.

**The *Michels* Class Action and Notice**

In 1995, the law firm Milberg Weiss Bershad Hynes & Lerach initiated a class-action lawsuit in New York state court against Phoenix, captioned *Michels v. Phoenix Home Life Mut. Ins. Co.*, Index No. 5318-95 (N.Y. Sup. Ct. Albany Cty.).

In August or September 1996, the Trustees and the Masons received notice of the *Michels* action and of a settlement reached in that action. The notice materials described four claims being asserted in *Michels*, along with Phoenix's response:

- How Phoenix used a method of using dividends to pay premiums on whole-life and Optionterm

policies. Phoenix responded that the vanishing premium concept of using dividends to offset premiums is common, and that Phoenix's sales material did not guarantee a specific level of dividends.

- Portraying life insurance as an investment. Phoenix responded that life insurance can be an appropriate way to meet savings, investment, or retirement goals.
- Funding a new policy by using an existing policy's cash value. Phoenix responded that such a method can be appropriate to meet financial goals.
- Failing to disclose risks associated with calculation of dividends. Phoenix responded that it fairly explained to policyholders how dividends were calculated.

Nothing in the notice referred to SLP policies or to claims that Phoenix misrepresented the projected premiums on those policies. (Phoenix had issued 6,791 SLP policies with Optionterm in the period covered by the *Michels* action.) Class counsel never raised an issue about Optionterm in the underlying suit; rather, it was Phoenix that "crafted" Optionterm into the settlement, noting in an internal communication, "It was something we were concerned about because we knew there would be issues." Phoenix later acknowledged that the *Michels* notice contained no specific information that would have allowed the Trustees and the Masons to make an informed decision regarding potential claims concerning payments required after the death of the first insured on an SLP policy. (App. 67). Nonetheless, the back pages of the *Michels* notice recited a two-and-a-half page "Release" whereby class

members who did not opt out of the action would be barred from asserting claims "that have been or could have been asserted in this lawsuit," including claims arising from misrepresentations about the "terms" of their policies and misrepresentations relating to the settlement agreement.

The opt-out period expired on October 18, 1996. The settlement provided that class members who did not opt out and did not elect a limited alternative dispute resolution ("ADR") option for those who could establish a misrepresentation would receive some temporary dividend enhancements and a temporary offset for any out-of-pocket payments needed to maintain Optionterm coverage.

The Trustees and the Masons contended below that after they received the notice, they contacted Phoenix's agent, who told them that the settlement did not adversely affect their policy and that they should not opt out.

After the *Michels* court approved the settlement in January 1997, the Trustees and the Masons received notice in April of a forty-five-day deadline for opting to choose the ADR or the default general relief. Earlier that year, they had received new projections, which again embedded the no-death scenario and showed that the policy was generally holding up as initially expected. Phoenix's agent advised the Trustees and the Masons not to elect ADR. Shortly thereafter (but before the ADR deadline), Phoenix generated internally, but did not disclose to its agent or to the Trustees and the Masons, projections showing that if Mr. Mason died at age eighty, premiums for the survivor rapidly escalated to hundreds of thousands of dollars annually, requiring total additional out-of-pocket payments of $4,984,325.

**The Litigation Below**

In 1999, the Trustees and the Masons finally received realistic projections for the policy premiums. They sued Phoenix in 2000. The trial court agreed with Phoenix that the Trustees and the Masons were bound by the *Michels* settlement as *res judicata* and by the Full Faith and Credit clause of the Constitution, and rejected their claim that the *Michels* notice was constitutionally inadequate. (App. 97). The Trustees and the Masons appealed, and a panel of the Pennsylvania Superior Court unanimously reversed, holding that under the facts claimed by the Trustees and the Masons, it was improper to rule as a matter of law that the notice satisfied due process. (App. 88). Phoenix appealed to the Pennsylvania Supreme Court, which reversed the Superior Court by a 4-2 vote.

On the due process issues, the majority opinion held (i) that the notice was facially adequate because it alerted the Trustees and the Masons to some potential problems with the policy involving a lack of disclosure by Phoenix and advised that the circumstances specified in the notice were not exclusive, thus placing "[t]he proverbial ball . . . in [the Trustees' and the Masons'] court to make an assessment of their own individual circumstance" (App. 34) and (ii) that "external fraud . . . cannot make this facially constitutionally adequate notice constitutionally inadequate." (App. 35).[1]

[1] The court then ruled in Phoenix's favor that under New York law the *Michels* judgment was not susceptible to attack under the narrow New York exception for fraud, and therefore was binding on the Trustees and the Masons under the Full Faith and Credit Clause.

In effect, the Pennsylvania Supreme Court ruled that (i) because class representatives claimed to have been misled regarding dividends and the "investment" nature of life insurance, the Trustees and the Masons, and other SLP class members, were on constitutionally adequate notice to make an "assessment" of whether Phoenix had misled them about the premiums owed on their policies, and (ii) in making this assessment, the Trustees and the Masons could not rely upon information provided directly to them by Phoenix as they were evaluating the settlement.

The dissenting opinion noted Phoenix's admission that the "notice was not complete with regard to either death scenarios or the escalating premiums," and concluded, "Coupled with the fraud demonstrated above, it defies common sense to determine that [the Trustees and the Masons] had adequate notice." (App. 68).

## REASONS FOR GRANTING THE PETITION

The Petition should be granted because the notice standard established in the decision below conflicts with this Court's precedents, is inconsistent with the standards established by two federal Courts of Appeals and a State supreme court, and presents important questions that should be settled by this Court.

### I. The Decision Below Conflicts with Precedents of this Court.

Modern class-action practice, whereby thousands or hundreds of thousands of people have their claims resolved, often in a distant forum, by a self-appointed

champion, has long presented conceptual and practical difficulties in applying the principles of due process.

One such difficulty occurs where the defendant seeks to take advantage of the settlement by consciously loading into the settlement documents an absolution for claims that are not described in the notice of settlement and are unknown to the class members.

In *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985), the Court held that a class action seeking money damages on behalf of the class could bind out-of-state members only if the members received notice that was "the best practicable, 'reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections.'" *Id.* at 812 (quoting *Mullane v. Cent. Hanover Bank & Trust Co.*, 339 U.S. 306, 314 (1950)). The notice must "describe . . . the plaintiffs' rights" and give each class member an opportunity not only to participate and object, but also to exercise the right to opt out of the class and protect his own interests, a right required by due process. *Id.* Applying that standard, the Court held that a "fully descriptive notice" plus the right to opt out satisfied due process. *Id.*

Although it cited *Phillips Petroleum*, the majority opinion below did not cite or apply the "best practicable" or "fully descriptive" standard or the requirement that the notice "describe . . . the plaintiffs' rights." (App. 32). Instead, the Pennsylvania Supreme Court held that due process was satisfied because the notice "alerted" the recipient that there were "potential problems" involving a lack of disclosure and that the specified circumstances were not exclusive. (App. 34). The notice thus supposedly

put "the proverbial ball" in the recipient's court to make its own investigation of whether there might be other problems. *Id.*

Beyond the failure to acknowledge the *Phillips Petroleum* "best practicable" standard, the Pennsylvania notice standard, which places on the recipient the burden of investigating whether he has undisclosed rights that are at risk, does not comport with the principles articulated in this Court's holdings regarding notice and due process generally. In *Mennonite Bd. of Missions v. Adams*, 462 U.S. 791 (1983), the Court held that "a party's ability to take steps to safeguard its interests does not relieve" the party intending to alter those interests of its due process requirements, noting that "a mortgagee's knowledge of delinquency in the payment of taxes is not equivalent to notice that a tax sale is pending." *Id.* at 799-800. *Griffin v. Griffin*, 327 U.S. 220 (1946), held that although a divorce and alimony decree put a party on notice that further proceedings to enter a judgment for the monetary award might take place, due process nonetheless required specific notice of the further proceedings. *Id.* at 229; *see also Schroeder v. City of New York*, 371 U.S. 208, 214 & n.6 (1962) (holding that knowledge of a change in a river's appearance did not satisfy due process requirement of notice to present claim for damages arising from a change in the river's velocity); *cf. In re Gault*, 387 U.S. 1, 34 (1967) (holding that due process does not allow a hearing "without . . . timely notice . . . of the specific issues that they must meet").

Moreover, the Pennsylvania notice standard disregards this Court's precedents by allowing the party giving the notice to withhold material information known to it

and unknown to the recipient, so long as the notice indicates that it does not identify all claims.

*Mullane* requires a court to consider "all the circumstances" in assessing notice, 339 U.S. at 314, and requires use of notice "such as one desirous of actually informing the absentee might reasonably adopt." *Id.* at 315. One desirous of actually informing a class member that valuable rights were being affected would not use the Pennsylvania-approved method of advising the class member of some claims that had been made against the settling defendant, while not mentioning other, more meaningful, claims known to the notice-giver but unknown to – in fact, concealed from – the class member.

Likewise, the further holding below that "extrinsic fraud . . . cannot make . . . facially constitutionally adequate notice constitutionally inadequate" (App. 35) not only makes the suggested "investigation" by the recipient impracticable, but disregards this Court's consistent holdings that notice is insufficient where the party giving notice knows that the recipient will not receive or understand it.

"In prior cases, we have required the government to consider unique information about an intended recipient regardless of whether a statutory scheme is reasonably calculated to provide notice in the ordinary case." *Jones v. Flowers*, ___ U.S. ___, 126 S. Ct. 1708, 1716 (2006) (referring to *Robinson v. Hanrahan*, 409 U.S. 38 (1972), and *Covey v. Town of Somers*, 351 U.S. 141 (1956)). *Robinson* held that notice was not "reasonably calculated" to inform a party when the sender knew that the party would not receive it. 409 U.S. at 40 (observing that notice was mailed to home address when intended recipient was in jail).

*Covey* held that notice was not sufficient when the sender knew that the recipient was incompetent to understand it. 351 U.S. at 146. *Flowers* held that a person "desirous of actually informing" the intended recipient would try again to send notice after he or she knew that the first attempt had not been received. 126 S. Ct. at 1716. The circumstances alleged below, where Phoenix or its agent told the Trustees and the Masons that the notice did not apply to their policy and then continued to feed them with misleading no-death premium projections, while at the same time withholding realistic projections, is not constitutionally distinguishable from those decisions.

Given this Court's holdings that a notice-giver's mere awareness that notice was not received or understood renders notice constitutionally inadequate, surely post-notice deception and concealment by the notice-giver must render the notice inadequate under the Due Process Clause.

## II. The Decision Below Is Inconsistent with Decisions by Several Federal Courts of Appeals and a State Supreme Court.

Other courts applying *Phillips Petroleum*, *Mullane*, or the "best notice practicable" standard of Federal Rule of Civil Procedure 23(c)(2) have adopted more rigorous standards for examining the content of class-action notices than the standard adopted by the Pennsylvania Supreme Court.

The Fifth Circuit in *In re Nissan Motor Corp. Antitrust Litig.*, 552 F.2d 1088 (5th Cir. 1977), established a standard for the "best notice practicable" under Federal Rule of Civil Procedure 23(c)(2). "[T]he substantive claims [must] be adequately described," and

> the notice . . . must contain information that a reasonable person would consider to be material in making an informed, intelligent decision of whether to opt out or remain a member of the class and be bound by the final judgment.

*Id.* at 1104-05.

Citing *Nissan*, the Eleventh Circuit in *Twigg v. Sears, Roebuck & Co.*, 153 F.3d 1222 (11th Cir. 1998), held as a matter of due process that class-action notices "needed to inform [the class member] as to whether claims *like his* were litigated in the [class] action." *Id.* at 1228 (emphasis added). The court held that a class-action notice identifying claims that Sears made "unnecessary and/or improper repairs" did not adequately describe a class member's claim that Sears completely failed to perform a promised service, *id.* (original emphasis omitted), and that the class member thus was not bound by a release of all claims that "were or could be asserted" against Sears in the class action. *Id.* at 1232 (setting forth text of notice describing release). In concluding the opinion, the court repeated that notice was inadequate because it did not "inform an absent class member like Twigg either that claims *like his* were being litigated or that they had been settled." *Id.* at 1228 (emphasis added).

The Eleventh Circuit standard would have led to a different result in the present case, as the *Michels* notice did not inform the Trustees and the Masons or other SLP policyholders that claims "like" theirs were being litigated or settled. Under the Pennsylvania standard, the Trustees and the Masons were left to figure out on their own that claims that they did not realize they had were being settled.

The Eighth Circuit, in *Reynolds v. Nat'l Football League*, 584 F.2d 280 (8th Cir. 1978), held that "[d]ue process requires that notice of a hearing to review the compromise of a class suit be structured in terms of content in a manner that enables class members rationally to decide whether they should intervene in the settlement proceedings or otherwise make their views known. . . ." *Id.* at 285. The *Michels* notice would not satisfy that standard as to SLP policyholders, because it is "structured in terms of content" at most to suggest to SLP policyholders that they should begin their own investigation of claims that they do not know about. The content of the notice does not allow the recipients "rationally to decide" anything about intervening to protect claims that they do not know they have.

*Vermont v. Homeside Lending, Inc.*, 175 Vt. 239, 826 A.2d 997 (2003), considered the effect of a notorious class action in which many class members found themselves losing far more money than they recovered through the action. *Id.* at 1002-04. Applying *Phillips Petroleum*, the Vermont Supreme Court concluded, "We can think of no better example than this case of why the notice must contain a description of plaintiffs' rights." *Id.* at 1009. The court also held that for the "jurisdiction by consent" model of *Phillips Petroleum* to work, "class members had to be able to evaluate what they were consenting to." *Id.* at 1011.

Under the standards articulated in *Homeside Lending*, the *Michels* notice would not bind the Trustees and the Masons because the notice did not describe what rights of SLP policyholders like themselves were to be litigated or settled, and because the notice did not allow an evaluation of what they would be consenting to by remaining in the

class, instead placing on the class members the burden of unearthing information needed to make such an evaluation.

## III. The Court Should Settle these Important Questions Regarding Class-Action Settlement Notices.

Class actions are a limited exception to the "'deep-rooted historic tradition that everyone should have his own day in court.'" *Martin v. Wilks*, 490 U.S. 755, 762 & n.2 (1989) (citation omitted). Class actions can provide significant benefits to class members, defendants, and the courts, but can also create the risk that groups of class members might have irreconcilably divergent interests or that inattentive or collusive class representatives might bargain away valuable claims too cheaply, as perhaps was done here, where Phoenix "crafted in" Optionterm as part of the settlement even though it had not been raised as an issue by class counsel. Those dangers make it important for courts to give real scrutiny to the mechanisms protecting class members from neglect and exploitation, including notice.

"[O]nce a sword for plaintiffs, the modern class action is in some contexts increasingly becoming a shield for defendants. . . . [It] now often provides a means by which unsuspecting future claimants suffer the extinction of their claims even before they learn of their injury." John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 Colum. L. Rev. 1343, 1350 (1995).

Settlements in class actions present heightened concerns. Judge Weinstein has observed, "One of the most serious practical problems in class actions is that judges may lack information needed to assess the settlement,

given the courts' dependence on plaintiff and defense counsel for details of the settlement's anticipated implementation and impact, and of the class members' receptivity to its provisions." Jack B. Weinstein & Karin S. Schwartz, *Notes from the Cave: Some Problems of Judges in Dealing with Class Action Settlements*, 163 F.R.D. 369, 378-79 (1995). With diminished judicial involvement, settlements present enhanced opportunities for collusion between class counsel and defendants.[2]

In a class-action settlement, then, the class members need meaningful tools to protect their own interests, and notice and opt-out rights are even more essential to the absent members than in a fully litigated case. "If implied consent is to be derived solely from failure to respond to

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[2] *See, e.g.*, Susan P. Koniak, *How Like a Winter? The Plight of Absent Class Members Denied Adequate Representation*, 79 Notre Dame L. Rev. 1787, 1797-98 (2004):

> There is a trade to be made here: a settlement offer with clear sailing on substantial fees for class counsel in exchange for a chintzy settlement for a large class and a wide release. But that deal is at the expense of the group not at the table: the absent class. Indeed, the requirement that a judge approve any class settlement is largely, if not completely, a recognition of the serious likelihood of just such collusion. . . .
>
> The judge is thus at a distinct disadvantage, not having been present at the table every step of the way. She has no reliable way to discern in which nook or cranny (of usually quite complex deals) evidence of collusion may lie. She may not even know what she should be looking for; i.e., what a non-collusive deal would provide. By and large she knows just what she is told. And the telling is not done by adversaries presenting clashing views on the settlement's fairness or the adequacy of the representation provided (or on any other matter on which she is required to rule, such as the adequacy of the notice) (footnote omitted).

class notices, courts will have to be a good deal more vigilant than they have been in scrutinizing the content of these notices." Henry Paul Monaghan, *Antisuit Injunctions and Preclusion Against Nonresident Class Members*, 98 Colum. L. Rev. 1148, 1186 (1998). "Notice of a class action – however communicated – must, at a minimum, be capable of communicating (to the one to whom notice is directed) what interest of his is before the court." Kozniak, *How Like a Winter?*, 79 Notre Dame L. Rev. at 1830 n.230.

Accordingly, the Court should take this opportunity to confirm that due process in a class-action settlement requires notice that meaningfully identifies the claims at issue and discloses material information about those claims known to the defendant seeking the benefit of the settlement.

## CONCLUSION

For the foregoing reasons, the petition for writ of certiorari should be granted.

Respectfully submitted,

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**[J-88-2005]**
**IN THE SUPREME COURT OF PENNSYLVANIA**
**WESTERN DISTRICT**

**CAPPY, C.J., CASTILLE, NIGRO, NEWMAN, SAYLOR, EAKIN, BAER, JJ.**

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| ANDREA D. WILKES, DAVID H. EHRENWERTH AND CHARLES K. CLARK, AS TRUSTEES OF THE MARK E. AND MYRNA L. MASON IRREVOCABLE TRUST, MARK E. MASON AND MYRNA L. MASON | : Nos. 11 & 12 WAP 2005 |
| v. | : Appeal from the Order of the Superior Court, entered May 26, 2004, at Nos. 126 WDA 2003 and 153 WDA 2003, reversing the Order of the Court of Common Pleas of Allegheny County, entered December 24, 2002, at No. GD 00-0745. |
| PHOENIX HOME LIFE MUTUAL INSURANCE COMPANY, A CORPORATION AND BALANCED EQUITIES, INC., A CORPORATION | : 851 A.2d 204 (Pa. Super. 2004) |
| APPEAL OF: PHOENIX HOME LIFE MUTUAL INSURANCE COMPANY, A CORPORATION | : ARGUED: September 12, 2005 |

## OPINION

**MR. JUSTICE CASTILLE DECIDED: JULY 18, 2006**

The primary issue on appeal is whether appellees Andrea D. Wilkes, David H. Ehrenwerth, and Charles K. Clark, trustees of the Mark E. and Myrna L. Mason Irrevocable Trust, and Mark E. Mason and Myrna L. Mason (collectively "appellees"), are barred by the doctrine of *res judicata* from bringing suit in Pennsylvania against appellant, Phoenix Home Life Mutual Insurance Company

("appellant" or "Phoenix"), due to an out-of-state class action settlement in New York. The Court of Common Pleas of Allegheny County granted summary judgment for Phoenix and dismissed appellees' suit, finding that since appellees had not opted out of a class action settlement filed in New York state court against appellant concerning the failure of some of its insurance policies to perform as promised, *res judicata* barred appellees from subsequently bringing suit against appellant in Pennsylvania on the same matter. On appeal, however, the Superior Court found that the class action notice apprising appellees of the New York settlement was constitutionally inadequate and reversed the trial court. This Court granted further review to determine the *res judicata* effect of the New York class action settlement, including the question of whether the class action settlement notice was constitutionally adequate. For the following reasons, we find that the Superior Court's decision was in error and, accordingly, we reverse that order and reinstate the trial court order granting Phoenix summary judgment.

In the late 1980s, Mark E. Mason and Myrna L. Mason ("the Masons") established a trust to purchase $7 million in life insurance that would enable the Masons' children to pay estate taxes without having to dispose of any illiquid portion of their estate. Andrea D. Wilkes, eldest daughter of the Masons, David Ehrenwerth, lawyer for the Masons, and Charles K. Clark, accountant for the Masons (collectively "Trustees"), were selected as the trustees for the trust. The Masons desired a policy where the premiums would diminish over time and, eventually, cease altogether at Mr. Mason's retirement, a point when the Masons would welcome fewer financial obligations.

Shortly after creating the trust, the Masons contacted independent insurance agent/broker Sander Lenenberg,[1] an acquaintance of the Masons since the 1970s, to obtain such a policy. Lenenberg suggested that the Masons purchase a whole life insurance second-to-die policy from appellant called a "Survivorship Life Protector" ("SLP"), with a rider referred to as "Optionterm," that would function as annual term insurance. Appellant advertised the proposed policy with phrases such as "quick pay," "rapid pay," and "vanishing premium." Theoretically under this plan, after premium payments had been made for fifteen years, the policy would produce enough dividends and paid-up additions[2] to obviate the need for further out-of-pocket premium payments. The targeted death-benefit value of the policy at the death of the second-to-die (i.e., Mark or Myrna) was $7 million. The proposed whole life insurance portion of the policy consisted of nearly $4.1 million, with the "Optionterm" rider contributing approximately an additional $2.9 million. Based on Lenenberg's projections, the base annual premium cost for the first five years would be $80,813, with the last of such payments required in 1993. The premium payments would

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[1] For purposes of this suit, appellees allege that Lenenberg acted as an agent of Phoenix.

[2] A paid-up addition is fully-paid additional insurance purchased through policy dividends.

> In essence, each year dividends are used to purchase small amounts of insurance protection for which no further premiums are needed. This additional protection can then be used to increase the death benefit payable on the policy. The cash value of these paid-up additions can also serve to reduce future premiums.

*Helping Your Client Choose the Right Life Insurance,* 42 NO. 7 PRAC. LAW. 29, 34 (1996).

then decline to $60,813 through 1999, and would diminish to $40,813 until the last premium payment in 2003. No premium payments would be owed after 2003. Lenenberg's projections did not illustrate any payment scenario to demonstrate what effect the first death of either Mark or Myrna Mason would have on the premiums.

In 1989, the Trustees purchased the SLP policy with the "Optionterm" rider. The policy summary showed that the face value of the whole life insurance was $4,117,647, and the "target face amount" of the "Optionterm" rider was $2,882,353. Insurance Policy Summary Schedule at 2. The total annual premium was listed at $80,813.23. *Id.* The policy also described how dividends generated by the policy could be used to reduce premiums and purchase paid-up additions. *Id.* at 9.

In 1994, the Trustees received a notice from Phoenix that the upcoming premium payment for the insurance policy was $80,813. Because the Trustees expected that the premium payments would reduce to $60,813 in 1994, Ehrenwerth wrote Phoenix inquiring about the discrepancy. Appellant responded by letter in April of that year:

> The proposals used in determining the "Quick Pay" date project dividends based on our current interest sensitive dividend scale and are neither guaranteed nor estimates of the future. Actual dividends payable may vary and will depend, to a greater extent than in the past on Phoenix Home Life's earnings on new investments.

Phoenix Letter to Trustees, April 22, 1994. The letter also provided a new illustration showing that the premium payments would last until the twenty-third year of the policy (as opposed to the fifteenth year) and decline at a

slower rate than initially expected. The Trustees then contacted Lenenberg about this letter and, subsequently, appellant reissued a new illustration conforming to the original proposal from 1989. Appellant provided the Trustees with more illustrations in June of 1994 that also matched their original expectations. None of the illustrations that appellant provided the Trustees in 1994, however, included and accounted for a first-to-die death scenario.

In January of 1995, an attorney working with Ehrenwerth's firm requested that Lenenberg review the policy and make projections that assumed dividends would be reduced by one and two percentage points. Phoenix later provided several illustrations in response to Lenenberg's inquiry on behalf of the Masons and the Trustees, but again none of the illustrations included a first-to-die death scenario. In March of 1995, Ehrenwerth contacted Lenenberg to inquire why the Trustees had received a notice stating that an additional $5,584.41 was owed on the policy, when Lenenberg had previously indicated that a payment of $60,813 would be sufficient for 1995. Because there were not enough paid-up additions in 1995 to account for the premium expenses in excess of the payment that the Trustees had made for that year, the Trustees took a loan on the policy, as suggested by Phoenix, to cover the balance due. In February and March of 1996, appellant produced additional illustrations to show how the premium payments would change if the Masons altered their out-of-pocket premium payments for a few years. Again, no death scenario was reflected in the charts provided.

In August or September of 1996, the Trustees received a notice concerning a proposed settlement of a New York

state court case involving a nationwide class action against appellant, *Michels v. Phoenix Home Life Mutual Ins. Co.,* Index No. 5318-95 (N.Y. Sup. Ct. Albany Cty. 1995). A cover-letter accompanied the notice, which stated that policyholders of policies purchased between 1980 and 1995 were affected, and also stated that the proposed settlement included an offset benefit for "Optionterm" policies.[3] The letter also outlined the two proposed settlement options for affected policyholders: either alternative dispute resolution ("ADR") or General Policy Relief (which is what appellees ultimately received).[4] Class members were encouraged in the letter to pursue further information: "If you have questions after reviewing this information, you can reach us at a special toll-free number we have set up with class counsel to answer your questions relating to the settlement, 1-800-556-8533." Cover Letter for *Michels* Proposed Settlement, at 1. Also, the date of the final hearing to approve settlement, November 8, 1996, was provided. *Id.* at 2.

A four-page question and answer brochure was included with the class action notice and it summarized the

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[3] The cover letter's opening paragraph stated that: "As a Phoenix policyholder who owned an individual, traditional whole life or universal life insurance policy between 1980 and 1995, you are considered a member of the class." Cover letter for *Michels* Proposed Settlement, at 1.

[4] The third page of the letter summarized the proposed benefits of the settlement, including: "Owners of in-force policies with Optionterm riders will *automatically receive:* **Optionterm Charge Offset** – A two-year offset of term insurance charges not otherwise covered by dividends." Cover letter for *Michels* Proposed Settlement, at 3. Accompanying information explained that this automatic relief would only be awarded if a policyholder chose the General Policy Relief at settlement, as opposed to ADR. Question and Answer Brochure for *Michels* Proposed Settlement, at 2.

details concerning the claims which were made in the suit and how policyholders would be affected by the settlement. The brochure explicitly noted that vanishing premium policies were implicated in the class plaintiffs' claims and that an offset for "Optionterm" policies automatically would be awarded in the settlement.[5] The "Optionterm" charge offset was delineated as follows:

> Class members will automatically receive the Optionterm Charge Offset if they (1) have in-force whole life policies with Optionterm riders and (2) do not elect to submit a claim to the ADR Process. Optionterm coverage is term insurance generally paid for by dividends. In some cases, dividends may in the future be insufficient to maintain coverage, and certain out-of-pocket payments may be required. If your policy has an Optionterm rider, the Optionterm Charge Offset will eliminate your out-of-pocket costs during the first two years for which an out-of-pocket outlay is required. (Class members will have the option of deferring the offset to the second and third years if they wish.)

Question and Answer Brochure for *Michels* Proposed Settlement, at 3. The brochure also provided the toll-free number established by class counsel to answer questions that any policyholder had with respect to the suit.

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[5] The brochure stated that the lawsuit involved claims concerning: "How the company sold vanishing premium polices, which Phoenix called 'Quick Pay' or 'Rapid Pay' policies. Vanishing premiums is a sales concept under which policy values, rather than out-of-pocket payments, are used to pay premiums on whole life policies. . . ." Question and Answer Brochure for *Michels* Proposed Settlement, at 1.

The settlement notice provided even greater detail concerning the class action, as it stated:

> The Plaintiffs make allegations concerning (i) how Phoenix made use of a method of using dividends to pay premiums on a whole life policy, or interest credited on a universal life policy, rather than paying them in cash, in order that no further out-of-pocket premium would be due after a fixed period of time, which sales concept was variously referred to as "Quick Pay" or "Rapid Pay," as well as Phoenix's use of dividends to help meet the costs of a rider known as Optionterm; (ii) the sale of life insurance by portraying it as an investment, savings, retirement or similar plan without disclosing that it is life insurance or the nature of the policy's benefits; (iii) the replacement of any existing life insurance policy with a new life insurance policy, or the sale of a new life insurance policy funded in whole or in part using an existing policy's cash value; and (iv) the failure to disclose material information in connection with the introduction of new methods for calculating dividends and crediting rates. The allegations in the lawsuits include claims that Phoenix misled policyowners in these and other circumstances.

Notice of Proposed Settlement for *Michels* Class Action, at 2. The notice warned that policyholders who failed to opt out of the settlement would be bound by its terms and policyholders in the class would be precluded from bringing any other lawsuit against appellant, specifically detailing that policyholders would be prohibited from making any claim about the number of premium payments required to keep the policy active. *Id.* at 11.

As to the benefits class members would have from the settlement, the notice explained that individuals with whole life policies would be eligible for "General Policy Relief," which could include dividend enhancements for up to four years, and the right to elect optimal premium loans through 2005. The notice also provided more detail as to how, under a General Policy Relief, offsets would be administered for policies with an "Optionterm" rider:

> The forms of relief available to class members under the proposed settlement are as follows:
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> 1. ***General Policy Relief.*** . . .
>
> * * *
>
> (c) ***Optionterm Offsets:*** Class members with in-force Policies having Optionterm riders will have an opportunity to receive the "Optionterm Offset." For all such class members, the Company will offset the out-of-pocket costs of their Optionterm riders during the first two years for which an out-of-pocket outlay is required to maintain existing levels of Optionterm coverage, unless the class member requests to delay such offset for one year. The purpose of the Optionterm Offset is to help class members maintain originally illustrated coverage that might otherwise require out-of-pocket outlay additional to that originally illustrated.

*Id.* at 6. For class members who did not believe that General Policy Relief would suffice, the ADR option was again offered and its procedures were explained in detail. *Id.* at 7-8. The toll-free number established to answer questions about the suit was provided multiple times, along with the address of counsel for the plaintiffs. None of the materials provided in the class action notice suggested

that policyholders should contact the agent who sold the policy for further information about the class action.

The Masons claimed that when they received the class action notice, they contacted Lenenberg, who told them that their policy was not affected by the proposed settlement and that they should not opt out. Whether Lenenberg rendered such advice was disputed below; however, the parties agree that the Masons remained part of the class action when the opt-out phase ended on October 18, 1996. In January and March of 1997, Phoenix provided the Masons and their Trustees, through Lenenberg, further illustrations detailing the future premium schedule payments, illustrations that closely resembled the initial payment schedule provided when the Trustees purchased the policy.

In mid-April of 1997, the Trustees received the details of the class action settlement which had been approved by the *Michels* court in an opinion dated January 3, 1997. The deadline for policyholders to choose their preferred method of relief (*i.e.,* General Policy Relief or ADR) was May 27, 1997. Appellees claimed that they again solicited Lenenberg's advice and Lenenberg advised them not to select the ADR option because their policy was not affected.[6]

On April 25, 1997, appellant internally produced another set of illustrations, unbeknownst to appellees,

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[6] The record reveals only that the Masons spoke with Lenenberg concerning which relief to invoke; there is no affirmative indication that the Masons returned the election form. However, it is apparent that they received General Policy Relief, which was the default if a putative plaintiff failed to opt-out or did not select ADR.

detailing what future premium payments would be owed in various circumstances. These illustrations included a "death scenario" which showed that if Mr. Mason died at eighty years-old, which would coincide with the twenty-first year of the policy, the out-of-pocket premium, which had vanished in the policy's thirteenth year, would return in the twenty-fourth year, when Mrs. Mason would be seventy-eight years old. To keep the policy in force through the forty-first year of its existence, in this scenario, Mrs. Mason would need to pay an out-of-pocket premium of $630,774. Appellees never received a copy of these illustrations.

In August of 1998, Mr. Mason discovered that Lenenberg was being investigated by the FBI for fraud perpetrated by misappropriating funds to himself that the Masons had paid on another insurance policy. The Masons responded by writing to appellant and requesting that a record of all transactions associated with their policy from its purchase be mailed directly to them, not via Lenenberg. On March 12, 1999, appellant sent Ehrenwerth a letter with 110 pages of illustrations, with all illustrations including the dividend enhancement benefit provided according to the General Policy Relief afforded in the class action settlement. One of the scenarios illustrated the premium payments if Mr. Mason died at age eighty-three. It showed out-of-pocket premium expenses returning in the twenty-seventh year of the policy and quickly escalating to exorbitant levels, such that the excess charge to keep the policy in force that year, in addition to the annual $80,813 premium, would be over $500,000. In that scenario, the total out-of-pocket premiums paid over the course of the policy would surpass $5 million.

Thereafter, the Trustees and the Masons filed a complaint against both Phoenix and Lenenberg's company, Balanced Equities, Inc.,[7] in March of 2000 asserting claims for breach of contract, fraud and deceit, negligent misrepresentation, reformation, violation of the Unfair Trade Practices and Consumer Protection Law, 73 Pa.C.S. § 20-1 *et seq.,* and bad faith under the Unfair Insurance Practices Act, 42 Pa.C.S. § 8371. In defense, appellant argued, *inter alia,* that the doctrine of *res judicata* barred the lawsuit, citing the *Michels* class action settlement in which the Masons had participated. The parties each filed motions for summary judgment in 2002 and, on December 23, 2002, the Honorable Judith Friedman of the Court of Common Pleas of Allegheny County granted appellant's motion on all claims. In a contemporaneous memorandum opinion, the trial court concluded that *res judicata* barred appellees' complaint as a result of the *Michels* class action because the prior settlement clearly covered the instant insurance policy. Trial court slip op. (December 23, 2002), at 1. The trial court further found that it was unreasonable for appellees to have relied on any representations that Lenenberg might have made concerning the class action's effect on the instant policy, stating, "[y]ou do not consult your enemy about how to interpret documents in dispute." *Id.* at 2. The trial court went on to note that if it were free to address the underlying merits of the action, the case would be ripe for resolution given that appellees had already paid premium payments higher than originally promised. The court also noted that there would be a

[7] Appellants never served Balanced Equities as a defendant, as it was effectively out of business due to Lenenberg's fraud prosecution, conviction and eventual imprisonment.

factual dispute regarding agency; specifically, whether appellant was liable for any misrepresentations made by Lenenberg. *Id.*

The Trustees and the Masons appealed and, on February 14, 2003, the trial court issued an opinion pursuant to Pa.R.A.P.1925(a). Trial court slip op. (February 14, 2003), at 1. In this opinion, the trial court reasoned that the *Michels* class action notice and accompanying brochure conveyed in plain terms that appellees' policy was implicated in the settlement, and that it was unreasonable as a matter of law for appellees to rely on the representations of Lenenberg and appellant, especially since there was no fiduciary relationship between appellees and appellant that might justify that reliance. *Id.* at 7-9.

On appeal, a Superior Court panel reversed and remanded in a published opinion. *Wilkes v. Phoenix Home Life Mutual Ins. Co.,* 851 A.2d 204 (Pa. Super. 2004). The panel began its legal analysis by articulating the elements of the *res judicata* doctrine under Pennsylvania authority, but then noted that without adequate class notice, a class member would not be prohibited by *res judicata* from relitigating claims resolved by a prior class action settlement. *Id.* at 210. The panel found that the *Michels* class action notice did not contain an adequate description to warn the Masons that their policy was affected by the impending settlement, because nothing in the notice mentioned the "second-to-die" policy that the Masons owned or made appellees aware that a "vanished premium for a second-to-die policy including an Optionterm component could reappear and quickly escalate." Moreover, the panel found that appellees could not possibly have been aware that they had been harmed by appellant, since they

did not realize anything was wrong with their policy at the time of the *Michels* settlement. *Id.* at 212-13.

The panel analogized appellees' case against appellant to *Amchem Products, Inc. v. Windsor,* 521 U.S. 591, 117 S.Ct. 2231 (1997), which involved a challenge to class action certification for settlement purposes in an asbestos exposure case. In *Amchem Products,* the propriety of class certification, under Rule 23 of the Federal Rules of Civil Procedure, arose because the class members included both individuals experiencing asbestos-related disability and individuals who only had been exposed to asbestos, but were not yet suffering from any asbestos-related medical condition. *Id.* at 602-03, 117 S.Ct. at 2239-40. Due to the differing interests of the two groups within the class, the Court held that the plaintiffs should not have been certified as a class. *Id.* at 625, 117 S.Ct. at 2250.

The panel viewed appellees here as being akin to the exposure-only claimants in *Amchem Products.* The panel then reasoned that it would be unfair to bar appellees' suit based on *res judicata* because: (1) Phoenix and Lenenberg had made several assurances that the policy would function as the Masons were originally told it would in 1989; (2) the *Michels* notice did not convey the potentially astronomical premium payments that could become due under the SLP policy; and (3) appellant's own corporate representative admitted that the *Michels* notice contained no information concerning the potentially large out-of-pocket premium payments required for an SLP policy after the death of the first insured. The panel then proceeded to hold that the notice of the *Michels* class action settlement sent to appellees was inadequate and, therefore, precluded a grant of summary judgment for appellant based on *res judicata. Wilkes,* 851 A.2d at 213. Moreover, with respect

to appellees' failure to opt out of the class action, the panel found that it was not unreasonable as a matter of law for appellees to rely on appellant's and Lenenberg's representations about the policy because appellant was the exclusive source of information concerning the policy's performance. In light of these findings, the panel reversed the grant of summary judgment in favor of appellant, and remanded the case to the trial court for it to reconsider its holding on the issue of fraud. *Id.* at 213-14.

This Court granted appellant's Petition for Allowance of Appeal, in an order dated April 12, 2005, to resolve the following issues:

> Whether, and to what extent, the doctrine of *res judicata* bars [appellees] from bringing suit in Pennsylvania under the instant circumstances?
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> Even assuming that *res judicata* bars [appellees'] underlying causes of action, whether the notice of class action settlement received by [appellees] was constitutionally adequate to fix [appellees'] rights in light of their decision not to opt out of the out-of-state class action suit?

*Wilkes v. Phoenix Home Life Mutual Ins. Co.*, 872 A.2d 1124 (Pa. 2005) (per curiam).

On appellate review, a trial court's grant of a motion for summary judgment will only be disturbed upon a finding that a genuine issue of material fact exists or where the moving party was not entitled to such a judgment as a matter of law. *Mullin v. Commonwealth, Dep't of Transp.*, 870 A.2d 773, 778 (Pa. 2005). In conducting our review, the record must be construed in a light most favorable to the non-moving party and any doubt as to the existence of a genuine issue of material fact must be

construed against the moving party. *Id.* 778-79 (citing *Hughes v. Seven Springs Farm, Inc.*, 762 A.2d 339, 340-41 (Pa. 2000)). We review pure matters of law *de novo*.

## I. *Res Judicata.*

Appellant first argues that *res judicata* bars appellees' suit because the *Michels* class action settlement is entitled to full faith and credit. Appellant claims that two other courts have already accepted this proposition in similar cases, namely, *Caputo v. Phoenix Mutual Life,* 723 A.2d 227 (Pa. Super. 1998) (unpublished decision), and *Cappuccio v. Phoenix Home Life Mutual Ins. Co.,* ATL-L-PP1497-94 (N.J. Super. Feb. 25, 1997) (unpublished decision). Appellant additionally contends that appellees' suit clearly would be barred under New York's *res judicata* doctrine and that, in this case, it is New York law that should be applied.

In response, appellees do not contest that a preliminary *res judicata* test would block their present claims; rather, they combat appellant's arguments by asserting that exceptions to *res judicata* apply. We will begin by first identifying the applicable *res judicata* doctrine.

The United States Constitution requires that full faith and credit "shall be given in each State . . . to the judicial [p]roceedings of every other State." U.S. Const. Art. IV, § 1. The Full Faith and Credit Clause thus precludes a party from attacking collaterally a judgment of one state by attempting to re-litigate the underlying dispute resolved by that judgment in another state. Thus, full faith and credit typically requires that a state give a judgment the same *res judicata* effect the judgment would have been afforded in the state in which it was rendered. *Thompson*

*v. Thompson,* 484 U.S. 174, 180, 108 S.Ct. 513, 517 (1988); *Durfee v. Duke,* 375 U.S. 106, 109, 84 S.Ct. 242, 244 (1963).

*Res judicata,* or claim preclusion, prohibits parties involved in prior, concluded litigation from subsequently asserting claims in a later action that were raised, or could have been raised, in the previous adjudication. *R/S Financial Corporation v. Kovalchick,* 716 A.2d 1228, 1230 (Pa. 1998). The doctrine of *res judicata* developed to shield parties from the burden of re-litigating a claim with the same parties, or a party in privity with an original litigant, and to protect the judiciary from the corresponding inefficiency and confusion that re-litigation of a claim would breed. *Id.*

Appellees do not dispute appellant's argument that this Court's inquiry into whether *res judicata* prohibits the instant suit should begin by applying *res judicata* doctrine as developed in the New York courts.[8] This Court's precedent on the question of which jurisdiction's *res judicata* doctrine should prevail in an instance in which the prior lawsuit arose in another jurisdiction has been unclear. For example, in *Commonwealth ex. rel. McClintock v. Kelly,* 134 A. 514, 516 (Pa. 1926), this Court applied its own *res judicata* doctrine to decide if the decision of a Maryland court should be provided *res judicata* effect. Nearly a half century later, however, this Court gave *res judicata* effect

[8] We note that, although appellees do not explicitly object to appellant's claim that New York *res judicata* law applies, and appellees devote a portion of their brief to discussing whether New York law distinguishes between extrinsic and intrinsic fraud, appellees also discuss the fraud exception as viewed by Pennsylvania courts. Appellees' Brief at 23-27.

to an Ohio judgment without applying Pennsylvania *res judicata* doctrine; there we rejected a challenge to the validity of an Ohio divorce decree. *Barnes v. Buck,* 346 A.2d 778, 782 & n. 11 (Pa. 1975). Although each opinion cites to the U.S. Supreme Court's Full Faith and Credit Clause jurisprudence, *McClintock,* 134 A.2d at 515-16; *Barnes,* 346 A.2d at 781, different approaches were ultimately employed in the two cases.

The divergence in view found in this Court's precedent is mirrored in the academic authority which exists on the question. Thus, some commentators have argued that the Full Faith and Credit Clause does not dictate that courts must employ the foreign state's *res judicata* doctrine in cases such as this. *See, e.g.,* Howard M. Erichson, *Interjurisdictional Preclusion,* 96 MICH. L. REV. 945 (1998) (analyzing different approaches to choice of law issue). It also has been argued that no authority precludes a state from using its own *res judicata* analysis when that state's preclusion law would give at least as much, or more, preclusive effect as the out-of-state court's law would mandate. *E.g.,* Comment, Gregory S. Getschow, *If At First You Do Succeed: Recognition of State Preclusion Laws in Subsequent Multistate Actions,* 35 VILL. L. REV. 253, 276 (1990); *see also* Gene R. Shreve, *Preclusion and Federal Choice of Law,* 64 TEX. L. REV. 1209, 1227-28 (1986) (discussing ability of federal courts to give greater preclusive effect to state court judgments). Finally, it has been argued that differing circumstances may warrant a court in declining to follow an immutable rule that the out-of-state's *res judicata* analysis must be used in every case. 18B ALAN WRIGHT ET AL., FEDERAL PRACTICE AND PROCEDURE § 4467 (2d ed. 2002) (providing several examples of

when it may be wise to depart from *res judicata* rules of out-of-state court).

On the other hand, there is ample authority weighing in favor of the proposition that the court should apply the *res judicata* law of the state that rendered the prior judgment. For example, the Restatement (Second) of Conflicts provides as follows:

> When a court has jurisdiction over the parties, the local law of the State where the judgment was rendered determines, subject to constitutional limitations, whether the parties are precluded from collaterally attacking the judgment on the ground that the court had no jurisdiction over the thing or status involved or lacked competence over the subject matter of the controversy.

RESTATEMENT (SECOND) OF CONFLICTS OF LAWS § 97 (1998). In addition, it is certainly safe to say that the U.S. Supreme Court and several state courts have generally applied the *res judicata* doctrine of the court where the judgment under collateral attack was rendered to determine if and when a collateral attack on that judgment is permissible. *See, e.g., Migra v. Warren City School District Board of Education,* 465 U.S. 75, 87, 104 S.Ct. 892, 899 (1984) (remanding to District Court to apply Ohio claim preclusion law); *Omega Leasing Corp. v. Movie Gallery, Inc.,* 859 So.2d 421, 424 (Ala. 2003) (looking to Virginia law to determine if judgment was final); *O'Connell v. Corcoran,* 770 N.Y.S.2d 673, 676 (2003) (according preclusive effect to Vermont divorce decree based on Vermont's *res judicata* law); *Jordache Enters., Inc. v. Nat'l Union Fire Ins. Co.,* 513 S.E.2d 692, 703 (W.Va. 1998) ("the full faith and credit clause generally requires the courts of this

State to give the New York judgment at least the res judicata effect which it would be accorded by the New York courts"); *Smith v. Shelter Mut. Ins. Co.,* 867 P.2d 1260, 1265 (Okla. 1994) (applying Arkansas claim preclusion law); *Nottingham v. Weld,* 377 S.E.2d 621, 623 (Va. 1989) (holding that Virginia courts must give federal court judgment same preclusive effect federal court would have given that judgment). *But see, e.g., Ditta v. City of Clinton,* 391 So. 2d 627, 629 (Miss. 1980) (applying preclusion law of Mississippi where Louisiana judgment was argued to have preclusive effect); *Finley v. Kesling,* 433 N.E.2d 1112, 1117 (Ill. App. Ct. 1982) (declining to apply collateral estoppel rules of Indiana).

The "fog of ambiguity" to which Mr. Chief Justice Cappy adverts in his concurrence, then, is a fog that is found both in our precedent and the commentary. Since the parties do not perceive or attempt to dissipate the fog, we are satisfied, in the present case, to indicate an awareness of the issue without purporting to offer, *sua sponte,* a definitive resolution. Therefore, consistently with the manner in which the case has been briefed to us, we will proceed by analyzing whether *Michels* would bar appellees' suit under New York law.

In New York, the doctrine of *res judicata* prohibits a party from litigating a claim where a judgment on the merits exists from a prior action between the same parties involving the same subject matter, including all claims that were litigated or could have been litigated in the prior action. *In re Hunter,* 794 N.Y.S.2d 286, 291 (2005).[9] Where

[9] It bears noting that it is not self-evident that the New York test for *res judicata* is coterminous with the approach prevailing in Pennsylvania. *See In the Matter of Dennis J. Iulo,* 766 A.2d 335, 337 (Pa.

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an action has reached a final conclusion, "all other claims arising out of that same transaction or series of transactions are barred, even if it is based upon different theories or if seeking a different remedy." *Id.* (quoting *O'Brien v. City of Syracuse,* 54 N.Y.2d 353, 357 (1981)) (internal quotations omitted).[10] A final order or judgment has been reached, under New York law, when all of the causes of action have been disposed of between the parties by the order or judgment and there is no need for further judicial action, excluding ministerial tasks. *Burke v. Crosson,* 623 N.Y.S.2d 524, 527 (1995). Finally, the New York Appellate Division has held that a judgment approving a class action settlement agreement is a final order for purposes of *res judicata. Sound Distributing Corp. v. Ponce Acquisition Corp.,* 577 N.Y.S.2d 863 (App. Div. 1992).

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2001) (*res judicata* bars subsequent action where "there exists an identity of issues, an identity of causes of action, identity of persons and parties to the action, and identity of quality or capacity of the parties suing or being sued.").

[10] To determine whether a claim is a part of the same transaction involved in a prior case, the New York Court of Appeals adopted the "transactional" test described in the Restatement (Second) of Judgments § 24(2). *See Chen v. Fischer,* 6 N.Y.S.3d 94, 100-01 (2005). Section 24(2) of the Restatement provides:

> What factual grouping constitutes a "transaction", and what groupings constitute a "series", are to be determined pragmatically, giving weight to such considerations as whether the facts are related in time, space, origin, or motivation, whether they form a convenient trial unit, and whether their treatment as a unit conforms to the parties' expectations or business understanding or usage.

*Id.* There is no issue in the case *sub judice* that the claims appellees would now pursue are part of the same transaction that gave rise to the *Michels* class action.

Here, when appellant sold its insurance policy to the Masons, the policy employed "quick pay" terminology and appellant referenced "quick pay" in correspondence with appellees. Letter from Phoenix to Trustees, dated 4/22/94. Hence, the Masons plainly were included in the class of plaintiffs in *Michels,* a lawsuit which brought various claims against appellant involving, *inter alia,* "quick pay" policies that would use accrued dividends to help meet the premiums of an "Optionterm" rider. Of the claims summarized in the class action notice, the first expressly accused appellant of misleading policyholders with regards to:

> a method of using dividends to pay premiums on a whole life policy, or interest credited on a universal life policy, rather than paying them in cash, in order that no further out-of-pocket premium would be due after a fixed period of time, which sales concept was variously referred to as "Quick Pay" or "Rapid Pay," as well as Phoenix's use of dividends to help meet the costs of a rider known as Optionterm. . . .

Notice of Proposed Settlement for *Michels* Class Action, at 2. The *Michels* court issued an eighty-four page opinion on January 3, 1997, addressing the adequacy of the class action settlement reached between appellant and Phoenix policyholders on this, and other, claims. Appellees now seek to challenge that same settlement on various grounds by re-litigating the claim brought in *Michels* involving "quick pay," an aspect of the Masons' SLP whole life insurance policy.

Viewing these circumstances in light of New York's *res judicata* doctrine, the instant matter plainly involves the same relevant parties as the prior suit, for appellees did not opt out of the *Michels* class action, and indeed, they

benefited from the settlement terms in that they were automatically entitled to receive a period of dividend enhancement, an offset of out-of-pocket premium costs for two years, and the right to elect optional premium loans through 2005. In addition, the present suit concerns the same subject matter as the class action; indeed, in both cases, the claims against appellant include allegations that it misled its policyholders into purchasing an insurance policy with the "quick pay" feature and the policy did not perform as promised. Moreover, a final judgment on the merits was rendered in *Michels,* as the New York court in that case rendered an opinion on the adequacy of the class settlement, which is deemed a final order under New York law. *See Sound Distributing Corp.,* 577 N.Y.S.2d at 863. Although appellees might take issue with the second prong of the test given their protestations, discussed *infra,* that the class action notice was inadequate because it did not explicitly mention SLP policies, that is not an allegation that would bear directly upon an element of the basic New York test for *res judicata.* And, indeed, appellees do not dispute that, absent the defective notice issue they wish to litigate, *res judicata* would bar this suit. Accordingly, in answer to the first question this Court accepted for review, we hold that appellees' suit presumptively would be barred by *res judicata* in a New York court and, consequently, we extend full faith and credit to the *Michels* judgment by preliminarily affording it that same preclusive effect in Pennsylvania.

## II. Adequacy of Notice.

Appellant next argues that the Superior Court erred when it declined to give the *Michels* judgment the preclusive effect it deserved on the separate ground of defective

notice, the defect consisting of the fact that the class action notice did not explicitly mention the SLP policy that the Trustees managed and the potentially astronomical premiums that might become due in certain scenarios. Appellant asserts that this Court's review of the adequacy of the class notice should be limited to accepting the *Michels* court's findings on the notice's adequacy, which appellant claims was extensive.

In the alternative, appellant argues that, even if this Court were to review the class notice *de novo,* the notice was adequate. Appellant emphasizes that the notice clearly explained that appellees would be subject to the terms of the class settlement if they failed to opt out of it, and that all known or unknown claims that may thereafter exist would be precluded by the settlement. In response to appellees' claim that the notice should have provided more information concerning their specific policy, appellant counters that appellees failed to seek further information by calling the toll-free number provided in the *Michels* notice and in the accompanying brochure. Appellant also notes the impracticality of the Superior Court's adverse decision, as it effectively would require that specific information pertaining to individual policies should have been disseminated to the 510,000 potential class members who were affected in *Michels.* Appellant submits that constitutional requirements respecting notice impose a more practical and less burdensome duty: class notice need only provide a reliable means for interested parties to become apprised of the pending action and an opportunity to present objections. Appellant argues that the toll-fee number provided this necessary forum for each potential plaintiff to learn what specific impact the class action would hold for an individual policy. Finally, appellant

argues that the fraud alleged should not have any effect on reviewing the adequacy of the class notice because appellees had notice and an opportunity to participate in the litigation, as well as warnings that they could not bring any claims against appellant in later litigation.

In response, appellees counter with the reasoning of the Superior Court that the current case is analogous to *Amchem Products,* where some of the class action plaintiffs had not yet suffered any physical harm and, accordingly, the Supreme Court held that the plaintiffs could not properly be certified as a class under federal civil procedure rules. In support of this reasoning, appellees point to appellant's failure to notify them of the effect that a death of one, but not both, of the Masons would have on future policy premiums. Appellees argue that the Superior Court rightly found that injury to the Masons had not manifested itself at the time of the settlement, that the class notice omitted necessary information, and that appellant deliberately prevented appellees from learning of the nature of the Masons' harm under the policy. In arguing defective notice, appellees specifically emphasize the absence of any mention of SLP policies in the class notice.

With respect to appellant's argument that this Court must defer to the *Michels* court's ruling on notice adequacy, appellees assert that this Court should not accept the premise, as it would allow the class action court to predetermine the *res judicata* effect of its own judgments.[11]

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[11] Appellees preliminarily argue that appellant waived its argument that this Court must accept the *Michels* court's ruling on notice adequacy, by failing to raise the argument below. In reply, appellant disputes this contention and cites passages from its Superior Court brief. Appellant claims that since appellees failed to previously dispute

(Continued on following page)

Appellees then summarize their position on the merits by arguing that review of the class action notice will prove it to be inadequate as to the Masons because appellant's fraud precluded appellees "from understanding the impact of the class action settlement on their claims." Appellees' Brief at 49.

As Chief Justice Cappy's concurrence notes, there is neither settled controlling authority nor even a consensus on the question of what level of deference a reviewing court should afford a settlement court's findings on the adequacy of class notice. The parties center their debate on two Federal Circuit Court cases. Appellant offers, and the Chief Justice prefers, the non-precedential view set forth by a single judge who authored the lead opinion in *Epstein v. MCA, Inc.*, 179 F.3d 641 (9th Cir. 1999) (Opinion Announcing the Judgment of the Court), for the absolutist proposition that this Court should engage in a "limited collateral" inquiry into the procedural aspects of the *Michels* court's ruling on notice adequacy. Appellees, on the other hand, cite *Stephenson v. Dow Chemical Co.*, 273 F.3d 249 (2d Cir. 2001), *aff'd in relevant part by an equally divided court*, 539 U.S. 111, 123 S.Ct. 2161 (2003) (per curiam), and argue that this Court should conduct a broad collateral review of the settlement court's findings. Appellees contend that, when a party argues that a court entered a judgment against it without authority, that party

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the notion that full faith and credit requires us to accept the *Michels* court's ruling on notice adequacy, appellees' waiver argument is itself waived. Appellant's Reply Brief, at 12-13. Given this Court's conclusion, *infra*, that we review challenges to an out-of-state court's ruling on the adequacy of class notice *de novo*, a conclusion that accepts appellees' substantive position, it is unnecessary to pass upon appellees' waiver argument.

is entitled to *de novo* review in the collateral proceeding. Appellees' Brief at 44-50.

In *Epstein,* a class of plaintiffs challenged the adequacy of legal representation in a Delaware state court class action settlement. The plaintiffs were included in that class and did not opt out of the settlement.[12] The settlement ended shareholder challenges to a tender offer that Matsushita Electric Industrial Co. made for MCA, Inc. In a lead opinion joined by neither of the two other judges on the panel,[13] Judge O'Scannlain opined that due process does not require a court to engage in "collateral second-guessing" when reviewing the settlement court's findings that support certification of a class settlement. *Epstein,* 179 F.3d at 648. Instead, Judge O'Scannlain wrote that a reviewing court should restrict itself "to consider whether the procedures in the prior litigation afforded the party against whom the earlier judgment is asserted a 'full and fair opportunity' to litigate the claim or

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[12] *Epstein* has a lengthy procedural history. When the plaintiffs first appeared before the Ninth Circuit, the court considered whether the plaintiffs' federal claims were barred by the Full Faith and Credit Act, 28 U.S.C. § 1738. *Epstein,* 179 F.3d at 643. The court determined that the settlement released claims within the exclusive jurisdiction of the federal courts. On further appeal, however, the U.S. Supreme Court determined that the Delaware judgment was entitled to full faith and credit. *Id.* On remand to the Ninth Circuit, a divided panel determined that the Delaware judgment was not entitled to full faith and credit because it violated due process given the inadequacy of class representation. *Id.* That opinion was later withdrawn and replaced with the opinion discussed in the text above. *Id.* at 644.

[13] Judge Wiggins concurred in the result reached by Judge O'Scannlain and filed an opinion to explain why he changed his vote from a prior appeal. Judge Thomas dissented and filed an opinion in which he objected to Judge O'Scannlain's failure to discuss whether the plaintiffs were even members of the class.

issue." *Id.* at 648-49. Judge O'Scannlain found support for his decision in *Phillips Petroleum Co. v. Shutts,* 472 U.S. 797, 105 S.Ct. 2965 (1985), stating that the Supreme Court never implied that a certifying court's determination of the adequacy of representation was subject to collateral review, and cited Federal Circuit Court cases for his view that class members' due process rights are protected by the certifying court and direct appeal courts. *Id.* at 648 (citing *Grimes v. Vitalink Communications Corp.,* 17 F.3d 1553, 1558 (3d Cir. 1994); *Nottingham Partners v. Trans-Lux Corp.,* 925 F.2d 29, 33 (1st Cir. 1991)). Furthermore, in concurring in the result, Judge Wiggins noted that the Delaware Chancery Court had already addressed individual class member challenges to the class representatives' representation. *Id.* at 651.

The situation confronting the Second Circuit Court of Appeals in *Stephenson* two years later was markedly different. In *Stephenson,* two veterans of the Vietnam War challenged a trial court's finding that their suit against manufacturers of the defoliant known as Agent Orange was barred by a 1984 settlement brought by service members disabled by the herbicide. *Stephenson,* 273 F.3d at 251. According to the class definition in the prior settlement, both *Stephenson* veterans were included within the class because they were members of the U.S. military, stationed in Vietnam between 1961 and 1972, and were injured by their exposure to Agent Orange. *Id.* at 260. The veterans had each been diagnosed with cancer in 1998, but were precluded from obtaining funds from the 1984 settlement because they had not claimed disability prior to 1994. *Id.* In a unanimous opinion, the Stephenson panel found that a party should not be foreclosed from collaterally attacking a class settlement when the party

claims to have been an improper party to the settlement under attack. *Id.* at 259. The attack was permissible, according to the court, since the adequacy of representation for class members manifesting injuries after 1994 had not previously been addressed and precedent supported such a collateral attack. *Id.* at 257-58. The court quoted *Hansberry v. Lee,* 311 U.S. 32, 61 S.Ct. 115 (1940), for the proposition that class action judgments can only bind members when their interests are unified, as well as the Second Circuit's previous pronouncement that class action judgments are not secure from collateral attack unless the absent members are vigorously represented. *Id.* at 258 (citing *Van Gemert v. Boeing Co.,* 590 F.2d 433, 440 n. 15 (2d Cir. 1978)).

The apparent divide between the approaches by Judge O'Scannlain and the *Stephenson* panel is likely a product of the differing tasks and factual circumstances facing the two courts. In *Epstein,* the dominant issue was the adequacy of class representation, while *Stephenson* pertained to the propriety of a class member's inclusion in the class which was subject to a prior settlement. In *Epstein,* the settlement court had already reviewed specific challenges to class counsel's representation, but in *Stephenson* the certifying and direct appeal courts had not previously addressed the interests of class members who became injured following the exhaustion of the 1984 settlement funds. Thus, the two approaches may not necessarily represent a schism in the law, so much as the reality that courts reviewing a collateral attack on a class settlement, and asked to balance judicial efficiency, finality of a judgment, and an individual's due process rights, may reasonably make different determinations in different circumstances. Class actions do promote judicial efficiency

by resolving claims shared by a large number of individuals when they are respected as final. On the other hand, we believe it unwise to adopt a prescriptive rule that would prevent going behind a class action judgment, but for procedural irregularities in that first judgment, irrespective of the specific claim forwarded. When a class member collaterally attacks a class settlement by alleging that he was wrongfully included in the class, an argument not made in *Epstein,* we believe the allegation should be permitted substantive collateral review because a class settlement does not always protect the interests of every party subject to it. *See Stephenson,* 273 F.3d at 259.

In the instant matter, the parties cite no case that specifically addresses the appropriateness and scope of collateral review when class notice is allegedly inadequate. However, the present case is sufficiently analogous to *Stephenson* to permit substantive collateral review here, as appellees' allegation (taken at face value for purposes of deciding our review paradigm) is premised on the notion that **nothing** in the class notice would have alerted them to the fact that they were inappropriately included in the class and the *Michels* court never addressed whether notice was adequate for class members with SLP policies. Inadequate notice, in fact, is a recognized exception to the effect of the *res judicata* doctrine. *See Kealoha v. Castle,* 210 U.S. 149, 155, 28 S.Ct. 684, 687 (1908). Moreover, this Court has previously noted that, in light of the requirements of due process, we are not obliged to give full faith and credit to a judgment of another state where notice was inadequate. *See Barnes,* 346 A.2d at 782 (citing *Hanson v. Denckla,* 357 U.S. 235, 78 S.Ct. 1228 (1958) and

RESTATEMENT (SECOND) OF CONFLICTS OF LAWS § 104 (1971)).[14] To ensure that this Court renders an independent judgment on this constitutional question, we believe that a broad collateral review of the notice is warranted for the limited purpose of assessing the appropriate *res judicata* effect. Furthermore, it is not entirely clear to us that the inquiry into adequacy of notice for class action purposes is coterminous with the inquiry into notice for purposes of *res judicata;* this is an additional reason weighing in favor of an independent review.

It is settled that notice is a fundamental requirement of due process, for a proceeding to be respected as final. *Mullane v. Central Hanover Bank & Trust Co.,* 339 U.S. 306, 314, 70 S.Ct. 652, 657 (1950); *Pennsylvania Coal Mining Ass'n v. Insurance Dep't of Pa.,* 370 A.2d 685, 692 (Pa. 1971). Notice is deemed adequate when it is reasonably calculated to inform a party of the pending action and provides the party an opportunity to present objections to the action. *Mullane.* Additional requirements have been articulated for notices sent in class actions. A potential plaintiff in a class action must be:

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[14] As the Restatement explains in a Comment, courts are not required to give judgments full faith and credit when they are rendered in violation of due process:

> Due process forbids the rendition of a judgment within the United States unless the State of rendition has judicial jurisdiction (see § 24) and unless the parties have been given adequate notice and adequate opportunity to be heard (see § 25). A judgment rendered in violation of these requirements is void in the State of rendition itself, and due process forbids the recognition and enforcement of such a judgment in sister States (see § 92).

RESTATEMENT (SECOND) OF CONFLICTS § 104, at Comment (a).

> provided with an opportunity to remove himself from the class by executing and returning an "opt out" or "request for exclusion" form to the court. Finally, the Due Process Clause of course requires that the named plaintiff at all times adequately represent the interests of the absent class members.

*Phillips Petroleum Co.*, 472 U.S. at 812, 105 S.Ct. at 2974.

On several occasions, this Court has explored the specific notice requirements demanded by due process. We have explained that the approach to determining what notice is adequate must be flexible and non-technical. *Harrington v. Dep't of Transp., Bureau of Driver Licensing*, 763 A.2d 386, 391-92 (Pa. 2000). Furthermore, we have noted that due process does not confer upon an individual the right to be deliberately obtuse to the nature of a proceeding. *See, e.g., Crooks v. Dep't of Transp., Bureau of Driver Licensing*, 768 A.2d 1106, 1109 (Pa. 2001).

Applying these principles, we have no difficulty in rejecting appellees' contention that the notice sent to them concerning the *Michels* class action did not provide them with sufficient information to comprehend the propriety of their inclusion in that litigation. First, as previously stated the cover-letter accompanying the notice not only stated that policyholders who purchased policies from 1980 to 1995 were affected, but it also mentioned that the proposed settlement included an offset benefit for "Option-term" policies. The letter specifically noted a toll-free number created by class counsel to answer questions that any policyholder had with respect to the suit and gave the date of the final hearing to approve settlement. Second, the four-page question and answer brochure made clear that the instant insurance policy was covered in the suit,

as it stated that vanishing premium policies were included in the plaintiffs' action, and that an offset for "Optionterm" policies would be automatically awarded in the settlement. The brochure, like the letter, also provided counsel's toll-free number for further information. Third, as mentioned in the above discussion on *res judicata,* the notice recounted the ways in which policyholders were allegedly "misled" by appellant, including appellant's: (1) offering policies that would use dividends to pay premiums on whole life insurance, "in order that no further out-of-pocket premium would be due after a fixed period of time, which sales concept was variously referred to as 'Quick Pay' or 'Rapid Pay,' as well as [appellant's] use of dividends to help meet the costs of a rider known as Optionterm;" (2) sale of life insurance under the guise it was an investment plan; and (3) failure "to disclose material information in connection with the introduction of new methods for calculating dividends and crediting rates." Notice of Proposed Settlement for Michels Class Action, at 2.

The notice also detailed that offsets would be given for individuals owning "Optionterm" polices and that "General Policy Relief" would be available for those with whole life insurance policies. Furthermore, the notice advised the putative class members of their right to opt out, and cautioned members about the consequences of failing to opt out of the suit, expressly warning that policyholders would be prohibited from making **any** claim about the number of premium payments required to keep the policy active. Notice of Proposed Settlement for *Michels* Class Action, at 11. Again, the toll-free number and addresses of class counsel were listed in the body of the notice.

Considering the breadth of information provided in the *Michels* class notice, question and answer brochure,

and cover-letter, appellees clearly were provided with sufficient information apprising them of the pending litigation and a means to present objections to it or to opt out. Due process requirements aside, notice is not an end in itself; in most instances, the recipient of notice must take some affirmative responsive action, whether it be investigation, a formal pleading, etc. The notice provided here alerted appellees to potential problems with their policy, that these problems involved a lack of disclosure by appellant, and that the specified circumstances in the notice were not exhaustive or exclusive. The proverbial ball was then in appellees' court, to make an assessment of their own individual circumstance, *i.e.,* to determine whether the class action adequately protected their interest. Notice is only the first step: the follow-up is generally a matter of individual responsibility. Thus, we hold that the notice in the case *sub judice* met the requirements of due process.

Moreover, we agree with appellant that the Superior Court's ruling would establish a higher due process requirement than is constitutionally necessary, at least as far as this case is concerned, in holding that the notice is constitutionally deficient for failing to specifically mention SLP polices. SLP policies were only one type of whole life insurance policy that might be adversely impacted by the vanishing premium policy option that was a primary claim in *Michels,* a claim that appellees were made amply aware of in the class notice. Due process does not require the notice to list every policy in which vanishing premiums are involved. Instead, an individual of reasonable intelligence could comprehend from the *Michels* notice that if he has an insurance policy with vanishing premiums, whatever the type of underlying policy, then that policy will be

affected by the class settlement and he should investigate to determine the best course in his individual circumstances. The Superior Court's approach would essentially require that the notice list every potential negative consequence of having a policy with "vanishing premiums" or "quick pay," such as the possibility for premiums to skyrocket for SLP policies. This requirement, we believe, is too burdensome – and it certainly is not required to satisfy basic notions of due process. It was sufficient to notify class members that "vanishing premium" policies were alleged by the plaintiffs in *Michels* not to operate as they were advertised.

Furthermore, we are unpersuaded by appellees' claim that fraud perpetrated by appellant precluded them from discovering the true scope of the *Michels* litigation. The class notice plainly provided appellees with the necessary information to understand that the Masons' insurance policy would be affected by the class settlement, if they failed to opt out of it, and even provided appellees with avenues to obtain further information, avenues they neglected to pursue. Simply put, the claim of external fraud forwarded here cannot make this facially constitutionally adequate notice constitutionally inadequate. We do not doubt that appellees now regret not having investigated the matter further when put on notice; but they cannot colorably claim they were unaware of the effect of their choice to surrender all claims.

Lastly, we are unpersuaded by the Superior Court's reliance on *Amchem Products.* In *Amchem Products,* the U.S. Supreme Court found that two provisions of Rule 23 of the Federal Rules of Civil Procedure prevented the putative class of plaintiffs, which included both individuals with asbestos-related disabilities and exposure-only

claimants, from being certified as a single class. First, Rule 23(b)(3) requires that class members share common questions of law or fact that "predominate over any questions affecting only individual members." The Court held that the class did not meet the predominance requirement, because exposure-only plaintiffs will incur different medical expenses for monitoring and treatment than plaintiffs already treating asbestos related diseases. 521 U.S. at 624, 117 S.Ct. at 2250. Second, the Court ruled that the putative class could not satisfy Rule 23(a)(4)'s requirement that the named parties fairly and adequately represent the class's interests, since class members currently suffering from asbestos disability would desire a immediate compensation for their injuries, whereas exposure-only claimants would be interested in preserving an ample fund for future possible expenses. *Id.* at 625, 117 S.Ct. at 2250. The Court also observed that the case raised important questions about the adequacy of class notice, but declined to rule on that issue because the class could not be certified. *Id.* at 628, 117 S.Ct. at 2252.

The Superior Court acknowledged that *Amchem Products* did not contain a holding directly related to the issue of adequate notice. *Wilkes,* 851 A.2d at 211. The panel nevertheless proceeded to find that appellees were like the exposure-only claimants in *Amchem Products,* who were unaware of their asbestos exposure and the potential health risk, because appellees "had no reason to believe they had or were being defrauded as they had received numerous assurances from Phoenix and Lenenberg that their policy coverage was as originally represented in 1989." Therefore, in the panel's view, appellees did not have the necessary information to decide whether to stay in or opt out of the class action. *Id.* at 213. But the

panel's finding in this regard is contradicted by the fact that the policy premium bill for 1994 was $20,000 more than the Masons expected, policy illustrations from 1994 showed the decline of premium payments occurring at a slower rate than initially expected, and the Masons had to borrow roughly $5,500 on their policy in 1995 to account for an unexpected premium payment shortage. While it is true that at the time the Masons had to decide whether or not to opt out of the class action they were unaware of the extent to which they might be defrauded in the future, they had ample evidence that their policy was not operating as advertised at the time the class action notice arrived. Thus, even assuming that *Amchem Products* would support a holding that class notice is deficient where it does not provide class members with sufficient information to determine whether they share in the injury alleged to have been caused by the defendant, it is of no avail to appellees here because they were given multiple indications that they had suffered the type of injury that was covered by the class action.

## III. Fraud.

Appellant's final claim is that appellees cannot succeed on a claim that fraud eviscerates the *res judicata* effect of the *Michels* judgment, unless appellees prove that class counsel in *Michels* was deceived, rather than proving fraud in relation to appellees' individual case. In the alternative, appellant argues that appellees were well aware that their policy was not operating as initially expected, they had opportunities to inquire about the class action's effect on the policy, and they never took reasonable steps to do so. Appellant argues that the only time period that is relevant to appellees' fraud claim is from August to

October of 1996, during the opt-out period, since appellees only claim fraud in inducing them to fail to opt out of the class action. Appellant further contends that any improper illustrations it provided to appellees before that time are irrelevant because claims of that nature were directly addressed by the *Michels* suit. Appellant lastly asserts that any fraud after October 1996 is likewise irrelevant.[15]

In response, appellees claim that *res judicata* does not bar the instant suit due to fraud committed by appellant. Appellees contend that it is a well-settled principle that fraud permits a collateral attack on a judgment and, here, fraud occurred during the settlement of the case. Construing the record in the light most favorable to the non-moving party, appellees argue, provides sufficient evidence for a jury to conclude that appellant defrauded them. Although Phoenix disputes that Lenenberg had an agency relationship with them, appellees claim that this relationship must be accepted as true for purposes of summary judgment. Moreover, appellees argue that appellant is not entitled to an inference that appellees were on notice of the policy defects, as appellees assert that they reasonably relied on appellant's false and misleading representations and their right to rely on these representations is a question of fact. Lastly, appellees dispute appellant's

[15] Because it found for appellees on the notice issue, the Superior Court did not address appellees' claim of fraud and, instead, directed the trial court on remand to reconsider the claim of fraud in light of the panel's findings on notice. *Wilkes*, 851 A.2d at 214. The fraud issue has been fully briefed here and is ripe for decision. In the interest of judicial economy, we will reach it. *See, e.g., Murphy v. Duquesne Univ. of the Holy Ghost*, 777 A.2d 418, 435 n. 12 (Pa. 2001). The question of whether summary judgment was appropriate on the fraud claim is one of law, hence our review is plenary.

contention that they must prove fraud occurred in connection with the *Michels* class action attorneys. Appellees argue that public policy requires that courts ensure that an individual plaintiff's rights in a class action are not sacrificed by "collusive attorneys;" therefore, courts must examine claims of fraud with respect to the individual class members. Appellees also assert that it is unrealistic to expect class members to actively contact class counsel and inform counsel of a defendant's and defendant's agent's representations to a class member.[16]

If a judgment has been procured by fraud or collusion, *res judicata* will not usually be an impediment to litigating a claim anew. *Morris v. Jones,* 329 U.S. 545, 550-51, 67 S.Ct. 451, 455-56 (1947). It appears that the highest court in New York has yet to apply the generally accepted principle that fraud is an exception to *res judicata,* but it has previously noted the existence of the exception. *See Parker v. Hoefer,* 142 N.E.2d 194, 196 (N.Y. 1957) (stating that fraud and collusion may generally operate as an exception to *res judicata,* while summarizing U.S. Supreme Court's case law on full faith and credit, but not discussing exception in relation to case).[17] Unsurprisingly, it also appears that the elements of fraud that a party

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[16] For the purposes of this decision, we will assume without deciding that a successful fraud claim may be maintained in relation to individual class members, rather than respecting class counsel. We do so because we find, *infra,* that the claim so viewed fails as a matter of law.

[17] Based on our earlier discussion concerning what state's claim preclusion law we should apply, in order to decide if the *Michels* judgment is entitled to full faith and credit, we analyze the present issue involving the contours of any fraud exception to the *res judicata* doctrine, under New York law.

seeking to re-litigate a claim must prove to gain the benefit of the fraud exception are left undefined. Considerations of comity weigh against attempting to delineate the specific boundaries of such an exception for New York and, consequently, we decline to sculpt and apply a specific fraud exception to *res judicata* here.

Rather, for present purposes, it is enough to note that we are satisfied that appellees could not successfully argue fraud as an exception to the *res judicata* doctrine in this case given New York's view of fraud cases generally. To establish a *prima facie* case of fraud in New York, one must allege a representation of a material fact, falsity, scienter, reliance, and injury. *See Small v. Lorillard Tobacco Co., Inc.,* 720 N.E.2d 892, 898 (N.Y. 1999). Moreover, reliance on a fraudulent misrepresentation must be reasonable. *See Hoffend & Sons, Inc. v. Rose & Kiernan, Inc.,* 796 N.Y.S.2d 790, 791-92 (App. Div. 2005); *Ruffino v. Neiman,* 794 N.Y.S.2d 228, 229 (App. Div. 2005).

Appellees' allegation of fraud in the case *sub judice* is advanced without any attempt to apply the allegation to a known legal standard or a suggested one. Taking appellees' allegations of fraud at their essence, this Court is asked to conclude that Lenenberg's assertions as appellant's agent (a fact, which we are required to consider as true for the purposes of summary judgment) that the instant insurance policy was not implicated in the *Michels* litigation undid the effect of the contents of the class notice, question and answer brochure, and accompanying cover letter. In our view, as a matter of law, appellees cannot succeed upon a claim of reasonable reliance on Lenenberg's statements when these statements directly conflict with the text of the class notice itself. *Cf. Ruffino,* 794 N.Y.S.2d at 229 (plaintiff not entitled as matter of law

to reasonably rely on misrepresentations when they directly conflict with terms of consent decree). This is particularly so considering the sophistication of Mr. Mason, a successful businessperson, and trustee Ehrenwerth, an experienced lawyer. Thus, even assuming that a fraud exception to *res judicata* would be accepted under New York law, we find that appellant is entitled to summary judgment on this claim.

For the foregoing reasons, we conclude that *res judicata* applies, that the class notice in this case was constitutionally adequate, and that the allegation of fraud is insufficient as a matter of law to defeat the effect of *res judicata*. Accordingly, we reverse the order of the Superior Court and reinstate the trial court's grant of summary judgment in favor of appellant. Jurisdiction relinquished.

Messrs. Justice Saylor and Eakin join the opinion.

Former Justice Nigro did not participate in the decision of this case.

Mr. Chief Justice Cappy files a concurring opinion.

Madame Justice Newman files a dissenting opinion in which Mr. Justice Baer joins.

Judgment Entered July 18, 2006

/s/ John A. Vaskov
Deputy Prothonotary

## CONCURRING OPINION

**MR. CHIEF JUSTICE CAPPY DECIDED: JULY 18, 2006**

I join the Majority Opinion in all respects save for its discussion of the purported choice of law issue regarding which state's issue preclusion law applies, as well as its treatment of the scope of review afforded to the settlement of an out-of-state class action suit.

Addressing the choice of law issue first, I see no reason to shroud the issue of which state's *res judicata* law would apply in this matter in a fog of ambiguity. *See Maj. Op.* at 15-17. In my view, Article IV, Section One of the United States Constitution, best known as the Full Faith and Credit Clause, and the pertinent jurisprudence of the United States Supreme Court, sweep away any uncertainty in this area and answer the issue definitively.[1]

The United States Supreme Court repeatedly has spoken to the purpose, policy, and function of the Full Faith and Credit Clause. The Court's view on these concepts is aptly summarized in *Underwriters Nat'l Assurance Co. v. N.C. Life & Accident & Health Ins. Guar. Ass'n,* wherein the Court stated:

> the concept of full faith and credit is central to our system of jurisprudence. Ours is a union of States, each having its own judicial system capable of adjudicating the rights and responsibilities of the parties brought before it. Given this structure, there is always a risk that two or more States will exercise their power over the same

[1] The Full Faith and Credit Act implements the protection of the United States Constitution's Full Faith and Credit Clause. 28 U.S.C. §1738.

> case or controversy, with the uncertainty, confusion, and delay that necessarily accompany relitigation of the same issue. Recognizing that this risk of relitigation inheres in our federal system, the Framers provided that 'Full Faith and Credit shall be given in each State to the public Acts, Records, and judicial Proceedings of every other State.' U.S. CONST., art. IV, § 1. This Court has consistently recognized that, in order to fulfill this constitutional mandate, 'the judgment of a state court should have the same credit, validity, and effect, in every other court of the United States, which it had in the state where it was pronounced.'

455 U.S. 691, 703-704 (1982) (quoting *Hampton v. McConnel,* 16 U.S. 234, 235 (1818)). The Full Faith and Credit Clause therefore upholds the integrity of a decision properly rendered in one state court by affording it the same effect in a sister state's court. In *Durfee v. Duke,* the Supreme Court stayed true to this principle, stating in clear terms that "full faith and credit thus generally requires every State to give to a judgment at least the *res judicata* effect *which the judgment would be accorded in the State which rendered it.*" 375 U.S. 106, 109 (1963) (emphasis supplied).

The Majority Opinion, however, claims this Court may speak to the issue of "determining which jurisdiction's *res judicata* doctrine should prevail in an instance in which the prior lawsuit arose in another jurisdiction." *See Maj. Op.* at 15. I find such a claim to be at odds with not only the Full Faith and Credit Clause of the United States Constitution and applicable precedent of the United States Supreme Court, but also with the role of this Court in following the construction and interpretation of the federal

Constitution. *Hall v. Pa. Bd. of Probation and Parole,* 851 A.2d 859, 863 (Pa. 2004) ("It is beyond cavil that this Court is bound by the determinations of the United States Supreme Court on . . . the construction and interpretation of the federal constitution.").

The Majority cites *Barnes v. Buck,* 346 A.2d 778 (Pa. 1975), as an instance illustrating this Court's vacillation in this area of the law. *See Maj. Op.* at 15 n.9. Respectfully, I differ with the Majority's reading of *Barnes,* as I view the *Barnes* decision to be in harmony with the well-settled principles set forth in *Durfee. See Barnes,* 346 A.2d at 363 ("The decree of the Ohio court . . . is entitled to full faith and credit in the courts of Pennsylvania . . . That is, we must give it the same recognition and *res judicata* effect as it would receive in the courts of Ohio.") In *Barnes,* this Court gave proper heed to the Full Faith and Credit Clause and the United States Supreme Court's construction thereof by determining if an Ohio court would have given preclusive effect to a prior decision from an Ohio court.[2]

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[2] Although I agree with the Majority's point that, in *Commonwealth ex rel. McClintock v. Kelly,* 134 A. 514 (Pa. 1926), this court used a Pennsylvania claim preclusion analysis to determine the effect of a prior Maryland decision, I do not think that *McClintock* is persuasive in illustrating this court's indecision as to which state's *res judicata* analysis applies. A close read of *McClintock* reveals that this court, like the Superior Court opinion in this matter, utilizes the Pennsylvania analysis without regard for the United States Supreme Court's Full Faith and Credit Clause jurisprudence. The *McClintock* decision, in this regard, is curious, as one of the federal cases it purports to rely upon, *Reynolds v. Stockton,* reiterates the well-settled rule in this area: "[F]ull faith and credit demanded is only that faith and credit which the judicial proceedings had in the other State in and of themselves require." *Reynolds v. Stockton,* 140 U.S. 254, 264 (1891).

The Majority further supports its contention that the law is unsettled as to whether the Full Faith and Credit Clause requires a state to apply the res judicata rules of the state rendering the judgment by citing to a variety of academic publications.[3] These academic sources do not add anything to the inquiry in this case as they each specifically support the general principle that a state must give the same preclusive effect to a judgment as would the rendering state. Regardless of the points that they espouse, commentaries from professors and law students, however learned, can in no way diminish the fact that both the Supreme Court of the United States and of this Commonwealth, as well as a good number of courts throughout the country, have spoken clearly to this issue, holding that the Full Faith and Credit Clause requires a state to apply the res judicata principles of the state rendering the judgment. See, e.g., *Durfee v. Duke, supra,* and *Barnes v. Buck, supra.*

As it is settled that the Full Faith and Credit Clause of the United States Constitution requires this Court to utilize New York's *res judicata* analysis in determining whether the decision in *Michels v. Phoenix Home Life Mut. Ins. Co.,* No. 5318-95, 1997 N.Y. Misc. LEXIS 171 (N.Y. Sup. Ct. January 3, 1997), bars Appellees' suit, I am unwilling to characterize this as a choice of law issue. Respectfully, therefore, I reserve myself from this discrete

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[3] The articles merely expound theories concerning peripheral issues such as, *inter alia,* whether a court may give a *more* preclusive effect to a judgment than the rendering state and whether a state is bound to give preclusive effect to the judgment of a federal court under the Full Faith and Credit Clause. As these articles address issues not present in this case, I am puzzled by their inclusion in the Majority's opinion.

portion of the Majority's analysis. Nevertheless, as the Majority indeed utilizes the New York *res judicata* formulation, as it must, I agree with the resolution of that facet of the opinion.

Similarly, while I agree with the result reached by the Majority with respect to Appellees' attack on the adequacy of the *Michels* settlement notice, I cannot agree with the proposition that this Court may engage in what the Majority terms a "*de novo*" review of the adequacy of the class notice in *Michels*. *See Maj. Op.* at 21 n.13, and 22. As the briefs in this matter reveal, there is a spirited debate amongst courts and commentators regarding whether a foreign court's class action due process determination[4] is subject to collateral review in another state court. *See* Appellants Brief at 32-41; Appellees' Brief at 44-50; Appellants Reply Brief at 14-17. Our Court has not yet addressed this issue. The Majority acknowledges this divide in its summation of the parties' arguments on this issue. Nevertheless, the Majority concludes in this matter of first impression that this court may engage in a "*de novo*" review.

As stated above, this issue is the focus of a scholarly dispute, as well as a split among both U.S. Circuit Courts of Appeal and state appellate courts. *See, e.g., Epstein v. MCA, Inc.,* 179 F.3d 641, 648 (9th Cir. 1999) (plurality opinion advocating narrow collateral review of rendering

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[4] Due process determinations by a class action court are those which the United States Supreme Court has deemed necessary to bind absent class members. *Phillips Petroleum v. Shutts,* 472 U.S. 797 (1985) (holding that notice, opportunity to be heard, a right to opt out, and adequate representation are necessary to bind absent class members to the judgment of the rendering class action court).

court's due process determinations); *Stephenson v. Dow Chemical,* 273 F.3d 249 (2d Cir. 2001) *aff'd in relevant part by equally divided court*, 539 U.S. 111 (2003) (permitting a merits-based attack by absent class members not specifically covered in prior determination); *Fine v. America Online, Inc.,* 743 N.E.2d 416, 421-24 (Ohio Ct. App. 2000) (adopting *Epstein*); *Hospitality Management Associates, Inc. v. Shell Oil Co.,* 591 S.E.2d 611 (S.C. 2004) (same); *State v. Homeside Lending, Inc.,* 826 A.2d 997 (Vt. 2003) (citing *Stephenson* with approval); Sara Mauer, Dow Chemical Co. v. Stephenson: Class Action Catch 22, 55 S.C.L.Rev. 467 (2004); 18A Charles Alan Wright, *et al.*, *Federal Practice and Procedure: Jurisdiction 2d* § 4455, at 486 (2d ed. 2002) (describing the *Epstein* position as reflecting "the deeper currents that are sweeping class litigation along towards uncertain destinations" and warning that *Epstein's* "new view . . . must confront many problems").

Appellants, on the one hand, advocate this Court to follow the *Epstein* line of decisions and thus limit Appellees' ability to collaterally attack the *Michels* court's ruling with respect to the adequacy of the class action notice approved by the New York court. According to *Epstein,* collateral second-guessing by courts outside of the original forum is inappropriate. Review by a second court under the *Epstein* model is limited to determining "whether the procedures in the prior litigation afforded the party against whom the earlier judgment is asserted a full and fair opportunity to litigate the claim or issue." *Epstein,* 179 F.3d at 648-49. Under this view, absent class members' due process rights are not protected by collateral review in a second court, but rather by the initial certifying court, direct appeal within that state's courts, and, ultimately,

the United States Supreme Court. *Id.* at 648, citing *Grimes v. Vitalink Communications Corp.,* 17 F.3d 1553, 1558 (3d Cir. 1994). The Ninth Circuit thus has held that "where the certifying court makes a determination of the adequacy of representation in accord with *Shutts* this determination is not subject to broad collateral review." *Epstein,* 179 F.3d at 648. As acknowledged by the South Carolina Supreme Court in *Hospitality Management,* important policy reasons support this limited type of review:

> It would run counter to the class action goals of efficiency and finality to allow successive review of issues that were, in fact, fully, and fairly litigated. Moreover, second guessing the fully litigated decisions of our sister courts would violate the spirit of full faith and credit.

*Hospitality Management Associates, Inc. v. Shell Oil Co.,* 591 S.E.2d at 659-60 citing *Fine,* 743 N.E.2d at 421.

Appellants claim the *Michels* court engaged in an extensive, in-depth analysis of the adequacy of due process protections, particularly with respect to the adequacy of the class notice. *See Michels,* 1997 N.Y. Misc. LEXIS 171, at *38-*54. Indeed, *Michels* recited the standard set forth in *Shutts,* and, after detailing the facts surrounding the adequacy of the notice provided therein, found "[t]he content and method of notice thus constituted due, adequate and reasonable notice to all Class Members and satisfied the requirements of due process, [New York's statute] and the Rules of this Court." *Id.* at *49-*50.

Conversely, Appellees advocate the approach adopted in *Stephenson,* which holds that a subsequent court may

engage in broad collateral review of due process determinations of the prior court. *See Stephenson,* 273 F.3d at 257-61. Appellees contend they are permitted to engage in a collateral attack on the *Michels* court determination that the notice was inadequate because of Phoenix's alleged fraud, and consequently, Appellees were never aware of any claims they may have had until after the opt-out period and after the relief made available under the Settlement Agreement was no longer available. Appellees argue that the *Stephenson* court found the notice inapplicable to the absent plaintiffs in that matter because the prior courts never made a due process determination targeted to them and therefore they were entitled to collaterally attack the due process determination. Appellees argue they are similarly situated to the absent plaintiffs in *Stephenson,* and therefore, the *Michels* determination on the adequacy of class action notice was not binding upon them.

The instant parties demonstrate their awareness and understanding of this schism. For example, Appellants dedicate several pages of their briefs to explaining the significance of the *Epstein* rationale and its adherents (*See* Appellants' Brief at 33-35; Reply Brief at 12-17); while Appellees' take lengths in diminishing *Epstein* and emphasizing the *Stephenson* rationale. (*See* Appellees' brief at 44-50). The Majority's approach is in accord with the approach espoused in *Stephenson.* Like *Stephenson,* the Majority engages in a broad, merits-based, or as it terms a "*de novo*" review of the notice question. I, however, would support a limited collateral review of this issue, one that comports with *Epstein.* The Majority attempts to support its approach by diminishing the instructive value of the Epstein opinion, claiming that it is but the "non-precedential

view set forth by a single judge who authored the lead opinion in *Epstein.*" Maj. Op. at 24. To the contrary, the rationale underlying the *Epstein* opinion has been discussed and recently adopted by the courts of two sister states. *Hospitality Management Associates, Inc. v. Shell Oil Co.,* 591 S.E.2d 611 (S.C. 2004); *Fine v. America Online, Inc.,* 743 N.E.2d 416, 421-24 (Ohio Ct. App. 2000).

The Majority further attempts to weaken the instructive value of *Epstein* in this case by asserting that it and *Stephenson* may "not necessarily represent a schism in the law" but rather, the two cases are products "of the differing tasks and factual circumstances facing the two courts." See, Maj. Op. at 27. To the contrary, courts and commentators view *Epstein* and *Stephenson* as espousing two contradictory legal tests as to the level of collateral attack permissible on a class action judgment:

> Thus it remains an open, and hotly litigated, question as to whether limited collateral review is required on the *Shutts* due process requirements in a class action case (*see Epstein III*), or whether a broader, merits-oriented collateral review is permitted (*see Stephenson*). In addition to the conflict in the federal circuits as exemplified by *Epstein III* and *Stephenson,* there is also disagreement amongst state courts and legal scholars.

*Hospitality Management,* 591 S.E.2d at 619. As there is a split in the law and this is a matter of first impression for this Court, our decision will have far-reaching consequences. I believe that the narrow review espoused by *Epstein* upholds the very principles underlying class action litigation, efficiency and finality, while also promoting judicial economy and comity with our sister states. As

such, I believe that this Court's holding should be in line with this approach.

Consistent with the *Epstein* approach, I would look to whether the *Michels* court adopted and followed adequate procedures to ensure that the due process rights of the absent plaintiffs were protected. The *Michels* court indeed engaged in an exhaustive review of the adequacy of the class notice, one that, in many respects, parallels that of the Majority. Because I am satisfied that the *Michels* court adopted the appropriate procedures for ensuring the due process rights of absent class members were protected, I am not willing to engage in collateral second-guessing. By this statement however, I am not subscribing to the view that a rendering court in a class action suit can insulate itself from review with a summary conclusion that the due process concerns were satisfied. In my view, the rendering court must engage in a substantive analysis of whether the rendering court established and employed the appropriate procedural safeguards in order for the absent plaintiffs to be bound by the determinations of the rendering court. If the rendering Court employed such an analysis, its determination should not be second-guessed by another court.

Given that the *Michels* court engaged in such an analysis, and my belief that limited collateral review is consistent with the spirit of the class action mechanism and the Full Faith and Credit Clause, I would find the *Michels* determination on the adequacy of the class notice to be binding upon Appellees. While the result I independently reach on this issue is similar to that of the Majority, I disassociate myself with the rationale underlying the Majority's conclusion in this regard.

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## DISSENTING OPINION

**MADAME JUSTICE NEWMAN DECIDED: JULY 18, 2006**

I respectfully dissent from the Opinion of the Majority. In particular, I find that based on the facts involved in the present matter, Appellees could prove fraud at trial and, as such, the doctrine of *res judicata* does not apply.

Two issues frame my discussion. First, this is a summary judgment proceeding. Therefore, we must review the record "in the light most favorable to the non-moving party, and all doubts as to the existence of a genuine issue of material fact must be resolved against the moving party." *Payne v. Dep't of Corr.*, 871 A.2d 795, 800 (Pa. 2005); *Pappas v. Asbel*, 768 A.2d 1089, 1095 (Pa. 2001). Second, it is well-established that the doctrine of *res judicata* does not apply where fraud may be found. *Morris v. Jones*, 329 U.S. 545, 550-51 (1947). "Where fraud is found, the party that used fraud should be deprived of the benefit of the judgment and any inequitable advantage gained. Courts should not forfeit truth for the sake of finality. . . ." *Leber-Krebs, Inc. v. Capitol Records*, 779 F.2d 895, 901 (2d Cir. 1985) (internal citation omitted); *see also In re Aegis Realty Corp.*, Nos. 02-16464 RDD, 03-10467 RDD, 2003 WL 22520394 (Bankr. S.D. N.Y. Oct. 31, 2003) (holding that, pursuant to New York law, a judgment of a court having jurisdiction of the parties and of the subject matter operates as *res judicata* only in the absence of fraud or collusion); *Bedrock Servs. v. Int'l Bhd. of Elec. Workers Local Union Nos. 238, 342, & 495*, 285 F. Supp. 2d 693, 698 (W.D.N.C. 2003) (noting that, without fraud or collusion, a judgment of a court having jurisdiction over the parties and over the subject matter operates as *res judicata*). Further, a judgment is not binding on a class

member where notice of the class action settlement was inadequate. *See Phillips Petroleum Co. v. Shutts,* 472 U.S. 797, 811-12 (1985) (citing *Mullane v. Cent. Hanover Bank & Trust Co.,* 339 U.S. 306, 314-15 (1950)). Such inadequate notice may be a result of the continued fraudulent acts of one party towards another specific party.

**Fraud**

My differences with the Majority center on the fraud allegedly committed by Appellant and its agent, Sander Lenenberg (Lenenberg), which makes the doctrine of *res judicata* inapplicable to the instant matter. The Majority states the standard as follows:

> To establish a *prima facie* case of fraud in New York, one must allege a representation of a material fact, falsity, scienter, reliance, and injury. *See Small v. Lorillard Tobacco Co., Inc.,* 720 N.E.2d 892, 898 (N.Y. 1999). Moreover, reliance on a fraudulent misrepresentation must be reasonable. *See Hoffend & Sons, Inc. v. Rose & Kiernan, Inc.,* 796 N.Y.S.2d 790, 791-92 (App. Div. 2005); *Ruffino v. Neiman,* 794 N.Y.S.2d 228, 229 (2005).

Maj. Slip Op. at 37. The Majority then goes on to misapply the test to the facts of this situation. In fact, the discussion and application of this test to the facts is cursory and consists of one paragraph dismissing the claim of Appellee.

The factual background governs the case *sub judice* and, as a result, I come to a different conclusion. The issue of which jurisdiction's *res judicata* doctrine should apply was not explicitly granted by this Court and was not briefed in full by both parties. Moreover, as noted by the Majority Opinion, this issue has not been fully addressed by this Court. Ultimately, I agree with both the Majority

by this Court. Ultimately, I agree with both the Majority and Chief Justice Cappy that we shall apply that of New York as both parties argued the issue on that basis. *Id.* at 15. I do not make a final judgment on the legal merits of the issue as to do so would be mere *dicta*.[1] Perhaps most importantly, the choice of law question is irrelevant in my final analysis, as fraud is clearly present in the facts as alleged. Consequently, to engage in a purely theoretical discussion concerning *res judicata* would be to remove focus from the egregiousness of the acts allegedly committed by the insurance company and its agent in this case. Further, I agree with the Majority's discussion of the scope of collateral review by this Court of the sufficiency of notice and its adoption of the approach in *Stephenson v. Dow Chemical,* 273 F.3d 249 (2d Cir. 2001), 539 U.S. 111 (2003) (permitting a merits-based attack by absent class members not specifically covered in prior determination). However, irrespective of which approach is used, that of the Concurring Opinion of Chief Justice Cappy, adopting

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[1] Mr. Chief Justice Cappy opines that, "[i]n *Durfee v. Duke,* the Supreme Court stayed true to this principle, stating in clear terms that 'full faith and credit thus generally requires every State to give to a judgment at least the *res judicata* effect *which the judgment would be accorded in the State which rendered it.*' 375 U.S. 106, 109 (1963) (emphasis supplied)." Concurring slip Op., C.J. Cappy, at 2. Further, his analysis of the Full Faith and Credit Clause of the U.S. Constitution, U.S. CONST., art. IV, § 1, accurately summarizes the history and importance of such a clause. *Id.* (citing *Underwriters Nat'l Assurance Co. v. N.C. Life & Accident & Health Ins. Guar. Ass'n,* 455 U.S. 691, 703-04 (1982) (quoting *Hampton v. McConnel,* 16 U.S. 234, 235 (1818))). Although his discussion is well-written and is a persuasive argument concerning the choice of *res judicata* doctrine, I cannot join it at this time because it is not properly before us. Again, as discussed *infra,* because fraud is found in the record as viewed in the light most favorable to Appellees, the matter should not be precluded or governed by the *res judicata* doctrine.

*Epstein v. MCA, Inc.*, 179 F.3d 641, 648 (9th Cir. 1999) (plurality opinion advocating narrow collateral review of rendering court's due process determinations), or that of the Majority using *Stephenson*, in the end, both the *res judicata* doctrine and the related review of adequate notice contain fraud exceptions to allow for full review of a claim settled in another jurisdiction.

In *Michels v. Phoenix Home Life Mut. Ins. Co.*, Index No. 5318-95 (N.Y. Sup. Ct. Albany Cty. 1995), the court addressed neither Appellees' allegations of fraud nor their factual scenario concerning ongoing fraud. Appellees' claim is highly factually specific, has not been addressed, and, if viewed in the light most favorable to Appellees as the non-moving party, vitiates the adequacy of the notice given because of the actions taken by Appellant to convince Appellees to ignore the otherwise potentially adequate notice.[2] Most important to our ability and need to review *de novo* the adequacy of the notice, no substantive review could have taken place regarding the adequacy of notice specific to Appellees.

As noted by the Majority:

> [T]he present case is sufficiently analogous to *Stephenson* [*v. Dow Chemical Co.*, 273 F.3d 249 (2d Cir. 2001)] to permit substantive collateral review here, as appellees' allegation (taken at face value for purposes of deciding our review

[2] In addition, I would err on the side of allowing review of the decision of another jurisdiction when it is possible that fraud, a different issue, or any other material difference exists. In particular, every care should be taken by this Court to protect the rights of Pennsylvania citizens and, thus, full review given where it either is or may be warranted.

> **ing** in the class notice would have alerted them to the fact that they were inappropriately included in the class and the *Michels* court never addressed whether notice was adequate for class members with SLP policies. Inadequate notice, in fact, is a recognized exception to the effect of the *res judicata* doctrine. *See Kealoha v. Castle,* 210 U.S. 149, 155, 28 S.Ct. 684, 687 (1908). Moreover, this Court has previously noted that, in light of the requirements of due process, we are not obliged to give full faith and credit to a judgment of another state where notice was inadequate. *See Barnes,* 346 A.2d [778], [] 782 [(Pa. 1975)] (citing *Hanson v. Denckla,* 357 U.S. 235, 78 S.Ct. 1228 (1958) and RESTATEMENT (SECOND) OF CONFLICTS OF LAWS § 104 (1971)). To ensure that this Court renders an independent judgment on this constitutional question, we believe that a broad collateral review of the notice is warranted for the limited purpose of assessing the appropriate *res judicata* effect. Furthermore, it is not entirely clear to us that the inquiry into adequacy of notice for class action purposes is coterminous with the inquiry into notice for purposes of *res judicata*; this is an additional reason weighing in favor of an independent review.

Maj. Slip Op. at 28-29 (footnote omitted). The fraud alleged in the case before us goes towards both the general fraud exception to the *res judicata* doctrine as well as the constitutionality of the notice. *See Morris, supra*; *Mullane, supra*. Accordingly, I turn to those facts I deem relevant.

The first problems came to the attention of Appellees in the sixth year of the policy, 1994, when the premium due was not reduced from $80,813.00 to $60,813.00. Accordingly, a trustee of Appellees wrote to Appellant on

January 28, 1994, and asked for confirmation of the reduced premium and for assurances that the policy was still in full effect.

At that time, Appellant sent a new illustration showing that the premiums would decline more slowly than in the original policy illustration and that expiration of the premiums would not occur in the sixteenth year of the policy but, instead, in the twenty-third year. Importantly, and apparently discounted by the Majority, is the fact that no death scenario was included in the illustrations. Appellees again contacted Appellant's agent, Lenenberg,[3] about the inconsistency, and a new set of illustrations was produced in April of 1994 showing the original payment schedule and the premium payments vanishing in the sixteenth year of the policy. Again, no death scenario was included.

Yet another set of illustrations was run in June of 1994 and provided to Appellees. Once again, the important factor is that no death scenario was included. In January 1995, a lawyer for Appellees reviewed the policy with Lenenberg and asked for an updated projection based on decreased dividends. As a result, in February of 1995,

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[3] I note that a dispute exists concerning the status of Lenenberg; namely, whether he is an Agent of either Appellant or Appellee or both. However, as discussed above, this is in the summary judgment phase, we must review the record "in the light most favorable to the non-moving party, and all doubts as to the existence of a genuine issue of material fact must be resolved against the moving party." *Payne v. Dep't of Corrections*, 871 A.2d 795, 800 (Pa. 2005); *Pappas v. Asbel*, 768 A.2d 1089, 1095 (Pa. 2001). Accordingly, I will address Lenenberg as the agent of Appellant until further notice. *Accord* Maj. slip Op. at 2 n.1 ("For purposes of this suit, appellees allege that Lenenberg acted as an agent of [Appellant]).

Appellant again supplied new premium schedules with reduced dividends and did not include a death scenario with the illustrations.

The following year, in February and March of 1996, Appellant supplied additional illustrations regarding varied premium payments but once more failed to include a death scenario. As such, Appellees understandably assert that they were led to believe that the original premium schedule would remain in effect regardless of the death of one party. However, Appellant had internal documents showing that it set the rates on the policy to reflect the dramatic change in actuarial status when one of the Masons died. Those rates were not disclosed to Appellees, and the information provided to them did not show that, if Mark Mason predeceased Myrna Mason, the previously vanished premiums would not only reappear but also escalate far beyond the original $80,813.00 premium.

In August or September of 1996, Appellees received notice of a proposed settlement of a nationwide class action brought in New York state court against Appellant. *See Michels v. Phoenix Home Life Mut. Ins. Co.,* Index No. 5318-95 (N.Y. Sup. Ct. Albany Cty. 1995). The notice itself did not clearly implicate Appellees' policy; instead, it included a four-page question-and-answer brochure that summarized the details concerning the claims made in the suit and how policyholders would be affected by the settlement. The brochure did explicitly note that vanishing premium policies were involved in the claim and that a settlement would include an offset for "Optionterm" policies. As quoted by the Majority, that offset provided:

> Class members will automatically receive the Optionterm Charge Offset if they (1) have in-force whole life policies with Optionterm riders and (2) do not elect to submit a claim to the ADR Process. Optionterm coverage is term insurance generally paid for by dividends. In some cases, dividends may in the future be insufficient to maintain coverage, and certain out-of-pocket payments may be required. If your policy has an Optionterm rider, the Optionterm Charge Offset will eliminate your out-of-pocket costs during the first two years for which an out-of-pocket outlay is required. (Class members will have the option of deferring the offset to the second and third years if they wish.)

Maj. slip Op. at 6-7 (citing Question and Answer Brochure for *Michels* Proposed Settlement at 3). A toll-free number was given if a policyholder wished to talk to class counsel concerning his or her policy in relation to the suit.

The notice of settlement provided further notice:

> The Plaintiffs make allegations concerning (i) how Phoenix made use of a method of using dividends to pay premiums on a whole life policy, or interest credited on a universal life policy, rather than paying them in cash, in order that no further out-of-pocket premium would be due after a fixed period of time, which sales concept was variously referred to as "Quick Pay" or "Rapid Pay," as well as Phoenix's use of dividends to help meet the costs of a rider known as Optionterm; (ii) the sale of life insurance by portraying it as an investment, savings, retirement or similar plan without disclosing that it is life insurance or the nature of the policy's benefits; (iii) the replacement of any existing life insurance policy

> with a new life insurance policy, or the sale of a new life insurance policy funded in whole or in part using an existing policy's cash value; and (iv) the failure to disclose material information in connection with the introduction of new methods for calculating dividends and crediting rates. The allegations in the lawsuits include claims that Phoenix misled policy owners in these and other circumstances.

*Id.* at 7 (citing Notice of Proposed Settlement for *Michels* Class Action at 2). In addition, policyholders were warned about the preclusion of certain claims if they chose not to opt out of the settlement. "The notice warned that policyholders who failed to opt out of the settlement would be bound by its terms and policyholders in the class would be precluded from bringing any other lawsuit against appellant, specifically detailing that policyholders would be prohibited from making any claim about the number of premium payments required to keep the policy active." *Id.* (citing Notice of Proposed Settlement for *Michels* Class Action at 11).

The Majority properly notes that the notice advised class members that they could opt out of the settlement until October 18, 1996, and thus not be bound by the settlement terms. Moreover, no recommendation was made to call the agent who sold the policy. *Id.* at 8. Appellees, however, did not contact the class action attorneys. Rather, they contacted Lenenberg, who falsely advised them that their policy was not affected and told them not to opt out of the class action. As a result, Appellees did not opt out. Thereafter, Appellant continued to provide Appellees with policy illustrations showing the same coverage as that originally represented in 1989.

In April of 1997, Appellees received a second notice indicating that class members who had not opted out of the *Michels* class action could either accept General Policy Relief or, if they believed that they could provide evidence of misrepresentation, could invoke an alternative dispute resolution (ADR) process. Appellees again contacted Lenenberg, who, for a second time, falsely advised them not to invoke ADR because their policy was not affected. "In January and March of 1997, Phoenix provided the Masons and their [t]rustees, through Lenenberg, further illustrations detailing the future premium schedule payments, illustrations that closely resembled the initial payment schedule provided when the [t]rustees purchased the policy." *Id.* at 8-9.

In my mind, great weight should be given to the fact that Appellant internally produced another set of illustrations including a "death scenario" showing that if Mr. Mason died at eighty years old the out-of-pocket premium that had previously vanished would return in the twenty-fourth year. The internal illustration also provided that, in order to keep the policy in effect, Mrs. Mason would need to pay up to $630,774.00 in additional out-of-pocket premiums. The Majority glosses over this internal representation and the fact that for several years Appellees had repeatedly requested documentation regarding their policy and were given false or incomplete illustrations each time. This illustration was prepared approximately one month prior to the deadline for invoking the Alternative Dispute Resolution (ADR) option in the class action suit but never given to Appellees. As such, it is unclear how Appellees would know that misrepresentation had occurred and that they should pursue the ADR option as all information

relevant to their specific policy was in the control of Appellant.

At this point in time, Appellants, through both the illustrations and representations of Lenenberg, had misrepresented material facts, including whether Appellees' policy was covered in the suit, the premium structure, and the hidden or non-disclosed scenario of death of one of the insured. Such representations were explicitly false or were reasonably relied upon to draw a false conclusion concerning Appellees' policy. The actions alleged were knowing in nature and made for the purpose of having Appellees reasonably rely upon the false information and directly resulted in an injury to Appellees of their inability to be fully compensated or opt-out of the settlement. *See Small v. Lorillard Tobacco Co., Inc.*, 720 N.E.2d 892, 898 (N.Y. 1999) (outlining factors governing fraud). Thus, Appellees have established a prima facie case of fraud pursuant to the alleged facts.

In August of 1998, Appellees learned for the first time that the FBI was investigating Lenenberg for fraud, which included Lenenberg diverting to himself substantial premiums that Mark Mason had paid for insurance with another insurance company. Upon learning this, Appellees wrote directly to Appellant and requested a complete history of all transactions concerning the insurance policy from its inception. On March 12, 1999, Appellees received from Appellant a letter with 110 pages of attached illustrations. All of the illustrations indicated that the policy was covered by the class action settlement, and some of the illustrations showed death scenarios with vanished premiums returning. This was the first time that Appellant provided illustrations revealing that vanished premiums would return upon the death of one spouse and, under

certain likely scenarios, would rise to exorbitant levels totaling up to $5,000,000.00 of total out-of-pocket premiums. Armed with this new information and the freshly provided illustrations, Appellees commenced the present suit alleging both breach of contract and, importantly for the *res judicata* argument, fraud.

The crux of Appellant's argument is that the Superior Court violated the Full Faith and Credit clause of the United States Constitution by failing to afford the *Michels* settlement and judgment *res judicata* effect and by reviewing *de novo* the adequacy of the class notice provided by the *Michels* court. Specifically, Appellant argues that the *Michels* court made express findings that the class notice satisfied minimal due process requirements, as required pursuant to *Phillips Petroleum Co. v. Shutts,* 472 U.S. 797 (1985), and that the Superior Court violated the Full Faith and Credit clause and statute, 28 U.S.C. § 1738, by disregarding that finding. *See Michels v. Phoenix Home Life Mut. Ins. Co.,* No 95/5318, 1997 WL 1161145 (N.Y. Sup. Ct. Jan. 07, 1997).

Appellant further asserts that, even if *res judicata* does not bar Appellees' underlying causes of action, the class notice provided by the *Michels* court was constitutionally adequate. Appellant maintains that the class notice fully informed Appellees of their rights and responsibilities as members of the class and of the details of the judgment and settlement. According to Appellant, the Superior Court erred by requiring the class notice to be narrowly tailored to Appellees' specific claims including the increased premiums upon the death of one of the insured.

Appellees counter that the class notice provided by Appellant was insufficient to enable them to make an informed decision about whether to opt out of the *Michels* class action. According to Appellees, Appellant defrauded them and attempted to obfuscate their injuries rather than notify them of their rights.

As the Superior Court panel noted, the appropriate threshold question in a case such as that *sub judice* is whether Appellees' suit is barred, in fact, by the doctrine of *res judicata*. *See Wilkes*, 851 A.2d at 210 (quoting *Taylor v. Shiley, Inc.*, 714 A.2d 1064, 1066 (Pa. Super. 1998)). However, where the initial lawsuit was in the nature of a class action, a plaintiff otherwise estopped by *res judicata* will not be barred from suing individually if the notice received by the plaintiff of the class action suit was not adequate to satisfy the constitutional demands of due process. *See Phillips Petroleum*, 472 U.S. at 811-12.

The threshold issue of whether *res judicata* barred the instant action was never fully addressed by either the trial court or the Superior Court. The doctrine of *res judicata* bars repetitious litigation of the same cause of action. As we have stated, application of this doctrine requires that the lawsuits possess the following common elements: (1) identity of issues; (2) identity of causes of action; (3) identity of persons and parties to the action; and (4) identity of the quality or capacity of the parties suing or sued. *Safeguard Mut. Ins. Co. v. Williams*, 345 A.2d 664, 668 (Pa. 1975).

However, a judgment procured by fraud is generally not entitled to *res judicata* or full faith and credit. *See Morris v. Jones*, 329 U.S. 545, 550-51 (1947). "Where fraud is found, the party that used fraud should be deprived of

the benefit of the judgment and any inequitable advantage gained. Courts should not forfeit truth for the sake of finality. . . ." *Leber-Krebs, Inc. v. Capitol Records,* 779 F.2d 895, 901 (2d Cir. 1985) (internal citation omitted).

Here, the facts of the case reveal that the judgment rendered against Appellees in the *Michels* class action was procured by fraud. Upon receiving notice of the *Michels* action, Appellees contacted Appellant's agent, Lenenberg, who on two separate occasions falsely advised Appellees not to invoke ADR because their policy was not affected. Moreover, during this same time period, Appellees received numerous assurances from Appellant and Lenenberg that their policy coverage was as originally represented in 1989 and would not be affected by the *Michels* action. I am not swayed by the Majority's statement that "[t]he trial court further found that it was unreasonable for appellees to have relied on any representations that Lenenberg might have made concerning the class action's effect on the instant policy, stating, '[y]ou do not consult your enemy about how to interpret documents in dispute.'" Maj. slip Op. at 11 (quoting Trial ct. slip Op. at 2). In particular, Appellees did not only rely on the statements of Lenenberg, who it should again be stated could be considered a dual-agent and not one of the enemy, but on the illustrations provided by Appellant. These are not interpretative matters but a clear allegation of fraud related to the disclosure of information held only by Appellant.

If proved at trial, such deliberate false representations to absent class members concerning their rights and options would clearly negate any boilerplate notice provided by Appellant in the *Michels* settlement. Accordingly, in light of Appellant's allegedly fraudulent misrepresentations, the

class action settlement and release in *Michels* does not preclude the present action filed by Appellees.

## Notice

Even if we ignore the fraudulent behavior of Appellant and assume that *res judicata* bars Appellees' underlying causes of action, a review of the facts shows that the notice of the class action settlement received by Appellees was not constitutionally adequate to fix Appellees' rights in light of their decision not to opt out of the out-of-state class action suit.

Adequate notice of a class action settlement is required by the constitutional mandate of due process. *See Mullane v. Cent. Hanover Bank & Trust Co.,* 339 U.S. 306, 314-15 (1950). As this Court has previously stated, notice is "the most basic requirement of due process." *Coal Mining Ass'n v. Ins. Dep't.*, 370 A.2d 685, 692 (Pa. 1977). To satisfy due process, notice of a class action settlement must be "reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections." *Mullane,* 339 U.S. at 314.

The Superior Court concluded that the trial court erred in granting Appellant's motion for summary judgment because a question of fact existed as to whether, under all of the circumstances of this case, the notice provided to Appellees was constitutionally adequate.

> [N]othing in the class action notice specifically referred to second-to-die policies, or to the possibility that a vanished premium for a second-to-die policy including an Optionterm component could reappear and quickly escalate.

Neither did anything in the notice disclose that after the two years of Optionterm Charge Offset had been funded by Phoenix, policyholders such as Appellants with a second-to-die policy could have to pay millions of dollars of out-of-pocket payments to maintain sufficient Optionterm coverage to meet a target amount of insurance projected, sold, and repeatedly illustrated even during the opt-out phase of the class action as requiring no out-of-pocket payment whatsoever.

¶ Significantly, Phoenix's own corporate designee, Robert Lautensack, admitted in his deposition that nothing in the class action notice provided specific information to enable the Masons and the Trustees to make an informed decision with respect to claims concerning out-of-pocket premiums required after the death of the first insured:

Q. I've already asked you this but I want to be sure it is covered, because it is one of the specific items in the corporate notice.

You indicated that there's no specific information within the class action notice to enable the plaintiffs – to make the Masons and trustees to make an informed decision with respect to claims concerning out-of-pocket premium payments required after the death of the first insured under the policy, is that correct?

A. That is correct.

(Deposition of Robert Lautensack, 10/30/01, at 189-90 (Exhibit F to Memorandum In Support of Plaintiffs' Motion for Summary Judgment, Vol. I) (R.R. 697a).) Paul Michael Fischer, Phoenix's Vice President of Life and Annuity, similarly testified that he did not recall the issue of out-of-pocket

> premiums due upon the death of the first insured being part of the settlement. (Deposition of Paul Michael Fischer, 6/28/02, at 219 (Exhibit D to Memorandum In Support of Plaintiffs' Motion for Summary Judgment, Vol. I) (R.R. 560a).)

*Wilkes,* 851 A.2d at 212. The Superior Court properly noted that, by Appellant's own admission, the notice was not complete with regard to either death scenarios or the escalating premiums. Coupled with the fraud demonstrated above, it defies common sense to determine that Appellees had adequate notice.

In addition, at the time of the *Michels* settlement, Appellees had no reason to believe they had been or were being defrauded because they had received numerous assurances from Appellant and Lenenberg that their policy coverage was as originally represented in 1989. Moreover, all records sent by Appellants concealed the true nature of Appellees' policy.[4] The Superior Court described the present situation in a logical manner considering the nature of this matter is one of summary judgment:

> [T]here was at least a question of fact regarding the adequacy of the notice, and it was not unreasonable as a matter of law for them to rely on Phoenix's representations under the circumstances, where they had an ongoing business relationship with Phoenix relating to the policy, Phoenix was the only source of information concerning their policy, and Phoenix was specifically

[4] In relation to the choice of law between New York and Pennsylvania, should the standards differ, I would be hesitant to apply a lesser protection standard to Pennsylvania citizens when it comes to protection from fraud.

> obligated to provide information about the class action by the terms of the settlement.

*Id.*

At the very least, because a question exists regarding the role of Lenenberg and the allegedly fraudulent and concealing activities undertaken by Appellant, the matter should not be dismissed at the summary judgment level and Appellees should be allowed to proceed to trial and attempt to prove fraud on the part of the insurance company. Specifically, Appellant and Lenenberg continued to provide Appellees with illustrations that showed the policy premiums vanishing, which was consistent with the policy's original explanation. Meanwhile, around the same time, Appellant was generating internal projections for the policy that showed exorbitant premiums upon the death of one beneficiary; yet it chose not to inform Appellees of these illustrations. Appellees did not know that this aspect of their policy varied from their original discussions and request for coverage. Nor did they have any reason to doubt the veracity of Appellant's and Lenenberg's representations until over one year after the period for invoking ADR ended. Appellant and its agent deliberately kept Appellees ignorant of their situation. As such, Appellees did not have the information or foresight needed to decide, intelligently, whether to stay in or opt out of the *Michels* class action or whether the notice of settlement applied to them.

Accordingly, I agree with the Superior Court that the trial court erred in granting Appellant's motion for summary judgment because a question of fact exists as to whether, considering all of the circumstances of this case,

the notice given to Appellees was constitutionally adequate.

## Conclusion

As the doctrine of *res judicata* does not apply in cases where fraud may be found, such fraud is currently alleged, and that fraud vitiates an already questionable notice, I would affirm the Superior Court. As such, I would remand to the trial court and allow the matter to proceed past the summary judgment stage and allow Appellees the opportunity to prove the alleged fraud.

Mr. Justice BAER joins this dissenting opinion.

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| ANDREA D. WILKES, DAVID H. EHRENWERTH AND CHARLES K. CLARK, as trustees of the MARK E. AND MYRNA L. MASON IRREVOCABLE TRUST, MARK E. MASON AND MYRNA L. MASON, | : | IN THE SUPERIOR COURT OF PENNSYLVANIA |
| Appellants | : | |
| v. | : | |
| PHOENIX HOME LIFE MUTUAL INSURANCE COMPANY, a corporate, and BALANCED EQUITIES, INC., a corporation, | : | |
| Appellees | : | No. 126 WDA 2003<br>No. 153 WDA 2003 |

Appeal from the Judgment Entered December 24, 2002
In the Court of Common Pleas, Civil Division
Allegheny County, No. GD 00-0745

BEFORE: FORD ELLIOTT, TODD, and TAMILIA, JJ.

OPINION BY TODD, J.: FILED: May 26, 2004

¶ 1 Appellants Andrea D. Wilkes, David H. Ehrenwerth, and Charles K. Clark, trustees of the Mark E. and Myrna L. Mason Irrevocable Trust (the "Trust"), and Mark E. and Myrna L. Mason appeal from the order of the Allegheny County Court of Common Pleas granting summary judgment in favor of Appellee Phoenix Home Life Mutual Insurance Company ("Phoenix"). We reverse, and remand.

¶ 2 The facts and procedural history of this case may be summarized as follows. In the late 1980's, the Masons,

who were then in their fifties, created an insurance trust to purchase and hold a $7 million insurance policy whose proceeds would enable the Masons' children to pay estate taxes without having to invade the illiquid corpus of the Masons' estate. The Trust named as trustees the Masons' oldest daughter, Andrea Wilkes, the Mason's lawyer, David Ehrenwerth, Esquire, and their accountant, Charles Clark (collectively, the "Trustees"). The Masons and the Trustees were seeking a policy whose out-of-pocket premium payments would cease by the time Mr. Mason retired, when the Masons would have less income available to fund premium payments, and that would avoid subjecting Myrna Mason to the financial burden of out-of-pocket premium payments in the event her husband predeceased her. To meet the Masons' needs, Phoenix's insurance agent Sander Lenenberg, with whom the Masons had been acquainted since the late 1970's, proposed that the Trustees purchase a Phoenix whole life second-to-die policy called "Survivorship Life Protector" ("SLP"), with a rider known as "Optionterm."[1] This type of policy was promoted by Phoenix on a "quick pay," "rapid pay," or "vanishing premium" basis, and contemplated that, after a specified number of premium payments, dividends and paid-up additions generated by the policy would be sufficient to make the policy self-sustaining so that no additional out-of-pocket payments would be due from the insured. The specific SLP policy proposed by Lenenberg for the Masons provided a targeted death benefit of $7 million on the

[1] The difference between Optionterm and the whole life component of the SLP insurance policy was that Optionterm was annual term insurance. Term insurance tends to be the most inexpensive form of life insurance when a person is young and the risk of death is low, but can become prohibitively expensive as a person ages.

death of the second-to-die, consisting of approximately $4.1 million of whole life insurance and $2.9 million of Optionterm. Under his proposal, which provided for a vanishing premium over time, the base premium for the coverage was to be $80,813 per year for the first five years of the policy, $60,813 per year beginning the sixth year and continuing until the tenth year, $40,813 per year from the tenth year until the fifteenth year, and finally to zero beginning in the sixteenth year of the policy (2004), and staying at zero thereafter. To support his proposal, Lenenberg provided the Masons and the Trustees with illustrations generated by Phoenix showing the out-of-pocket premium payments reducing to zero in 2004, and staying there. According to the Masons and the Trustees, these illustrations did not indicate that the death of one insured would have any impact on the premiums. Based on Lenenberg's proposal, the Trustees purchased the SLP policy in 1989 and began making the agreed-upon premium payments.

¶ 3 In January 1994, the Trustees received an annual premium notice indicating that the premium for the sixth year would be $80,813.23 rather than the decreased amount of $60,813. In light of this discrepancy, Trustee Ehrenwerth wrote to Phoenix on January 28, 1994 and asked them to confirm that the premium due was $60,813, and otherwise confirm that the policy remained in full force and effect. In response, Phoenix sent the Trustees a new illustration which showed the total out-of-pocket payment required declining more slowly than shown in the original illustration and not vanishing until the 23rd year of the policy. After the Trustees contacted Lenenberg about this inconsistency, and Lenenberg inquired of Phoenix, Phoenix ran a new set of illustrations on April 29, 1994 in

which the out-of-pocket premium payment schedule conformed to the original 1989 illustration, with premium payments declining and vanishing entirely in the sixteenth year of the policy. No death scenario was included in these illustrations. Phoenix ran another set of illustrations in June 1994 which were provided to Trustee Ehrenwerth and the Masons, again confirming the original premium schedule, but again also omitting a death scenario.

¶ 4 In January 1995, after receiving the policy anniversary statement, a lawyer for the trust reviewed the policy with Lenenberg and requested him to provide an updated projection for the policy that assumed dividends reduced by one and two percentage points. In February 1995, Phoenix ran seven illustrations showing a variety of scenarios with respect to premium schedules and dividend reductions, none of which showed a death scenario. In February and March 1996, Phoenix ran additional illustrations to determine what would happen if the Masons varied their out-of-pocket payments for a few years. Here again, no death scenarios were shown.

¶ 5 Appellants claim that while they were being led to believe the original premium schedule would be in effect regardless of which death scenario was employed, internally, Phoenix was setting its rates on the Mason's policy to reflect the dramatic change in actuarial status when one of the Masons died. According to those rates, which Appellants claim Phoenix never disclosed to them, under certain probable scenarios in which Mark Mason predeceased Myrna Mason, out-of-pocket premiums which had previously vanished would reappear and quickly escalate to hundreds of thousands of dollars per year.

¶ 6 In August or September 1996, the Trustees received notice of a proposed settlement of a nationwide class action brought in New York state court against Phoenix, ***Michels v. Phoenix Home Life Mutual Ins. Co.,*** Index No. 5318-95 (N.Y. Sup. Ct. Albany Cty. 1995). The class action notice described the allegations made in the ***Michels*** action as follows:

> The Plaintiffs make allegations concerning (i) how Phoenix made use of a method of using dividends to pay premiums on a whole life policy, or interest credited on a universal life policy, rather than paying them in cash, in order that no further out-of-pocket premium would be due after a fixed period of time, which sales concept was variously referred to as "Quick Pay" or "Rapid Pay," as well as Phoenix's use of dividends to help meet the costs of a rider known as Optionterm; (ii) the sale of life insurance by portraying it as an investment, savings, retirement or other similar plan without disclosing that it is life insurance or the nature of the policy's benefits; (iii) the replacement of any existing life insurance policy with a new life insurance policy, or the sale of a new life insurance policy funded in whole or in part using an existing policy's cash value; and (iv) the failure to disclose material information in connection with the introduction of new methods for calculating dividends and crediting rates. The allegations in the lawsuits include claims that Phoenix misled policyowners in these and other circumstances.

(Notice of ***Michels*** Class Action, August 1996, at 2 (R.R. at 1528a).)[2] The class action notice indicated that those who remained in the class and had whole life policies would be eligible to receive "General Policy Relief," consisting of dividend enhancements for up to four years and, if they had an Optionterm rider, they could receive "Optionterm Offset" which was a two-year offset of the out-of-pocket outlay required to maintain Optionterm coverage.

¶ 7 After the Masons and the Trustees received notice of the class action and proposed settlement, they consulted with Lenenberg whom they claim reassured them on behalf of Phoenix that their policy was not affected and advised them they should not opt out of the class action.[3] The Masons and the Trustees ultimately chose not to opt out, and the opt-out phase ended on October 18, 1996. In the months that followed, Phoenix continued to provide

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[2] The Questions and Answer Brochure that accompanied the class action settlement notice similarly described the lawsuit as involving, *inter alia,* Phoenix's alleged misrepresentations concerning its vanishing premiums program:

> **What claims were made against Phoenix in this lawsuit?**
>
> The lawsuit makes several claims about how certain types of policies were sold. Broadly, the lawsuit alleges misrepresentations involving sales practice claims, including the use of dividends to reduce out-of-pocket cash premiums. . . . Specifically, the lawsuit made four such claims:
>
> 1. How the company sold vanishing premium policies, which Phoenix called "Quick Pay" or "Rapid Pay" policies. Vanishing premium is a sales concept under which policy values, rather than out-of-pocket payments, are used to pay premiums on whole life policies. . . .

(Question and Answer Brochure, August 1996, at 1 (R.R. at 323a).)

[3] In his deposition, Lenenberg denied ever having advised either the Masons or the Trustees not to opt out of the class action.

the Trustees with policy illustrations which depicted the policy coverage as originally represented. In January and again in March 1997, for instance, Phoenix generated and provided to the Masons via Lenenberg illustrations confirming, with minor variations, the basic out-of-pocket premium payments and death benefit terms of the policy as originally represented in 1989.

¶ 8 In mid-April 1997, the Trustees received a notice indicating that class members had 45 days, or until May 27, 1997, to accept General Policy Relief or, if they believed they could provide evidence of misrepresentation, invoke the alternative dispute resolution ("ADR") process. After they received this notice, the Trustees and the Masons once again turned to Lenenberg for his advice. According to Trustee Ehrenwerth and Mr. Mason, Lenenberg told them not to invoke ADR because their policy was not affected.

¶ 9 Unbeknownst to the Trustees and the Masons, on April 25, 1997, Phoenix generated another set of illustrations for the Masons' policy which showed Mr. Mason dying in year 21 at age 80. In that illustration, the out-of-pocket premium vanished after the 13th year, but then returned in the 24th year when Mrs. Mason would be 78, and quickly escalated until it reached $630,774 for the 41st year. This illustration was never provided to the Masons or the Trustees.[4]

¶ 10 In August 1998, Mr. Mason learned for the first time that the FBI was investigating Lenenberg for fraud, which included Lenenberg diverting to himself substantial

[4] Lenenberg claimed in his deposition that he did not receive this illustration either.

premiums that Mason had paid for insurance with another insurance company. Upon learning this, the Trustees wrote directly to Phoenix and requested Phoenix to send directly to them, and not through Lenenberg, a complete history of all transactions concerning the policy from its inception. On March 12, 1999, after some prompting from the Trustees, Phoenix sent Trustee Ehrenwerth a letter with 110 pages of attached illustrations. All of the illustrations included the dividend enhancement benefit provided under the class action settlement. In one of the illustrations, which had Mr. Mason dying first at age 83 (year 24 of the policy), out-of-pocket premiums would return in year 27 of the policy when Mrs. Mason was 81 and quickly escalate to astronomical levels, resulting in Mrs. Mason having to pay over $5 million in out-of-pocket premiums just to keep the policy in full force. The Trustees and the Masons claim that this was the first time in ten years of providing illustrations that anyone from Phoenix had revealed that the vanished premiums would return and, under certain likely scenarios, would rise to exorbitant levels.

¶ 11 In March 2000, the Trustees and the Masons filed a complaint against Phoenix and Lenenberg's company, Balanced Equities, Inc.,[5] asserting claims for fraud, negligent misrepresentation, reformation, breach of contract, and violation of the Unfair Trade Practices and Consumer Protection Law,[6] and bad faith under the Unfair

[5] Although Appellants named Balanced Equities, Inc. as a defendant, it was never served as it was effectively out of business as a result of Lenenberg's fraud conviction and subsequent imprisonment.

[6] 73 Pa.C.S.A. § 201-1 *et seq.*

Insurance Practices Act[7] in connection with the sales and servicing of the Masons' policy. Phoenix asserted that Appellants' claims were barred by the ***Michels*** class action settlement. In the summer of 2002, the parties filed cross-motions for summary judgment and, on December 23, 2002, the Honorable Judith L.A. Friedman of the Allegheny County Court of Common Pleas granted Phoenix's motion for summary judgment as to all claims. These appeals followed.[8] In a subsequent opinion issued pursuant to Rule 1925(a) of the Pennsylvania Rules of Appellate Procedure, the trial court explained that Appellants' claims were barred by the ***Michels*** class action settlement on grounds of *res judicata* and full faith and credit because Appellants' reliance on Phoenix's representations concerning the ***Michels*** class action settlement was unreasonable as a matter of law.

¶ 12 Appellants present the following issues for our consideration, which we have paraphrased:

1. Did the trial court err in granting summary judgment in favor of Phoenix by finding, as a matter of law, that the ***Michels*** class action notice was constitutionally adequate?

2. Did the trial court err in granting summary judgment in favor of Phoenix on the alternative basis that Appellants could not show, as

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[7] 42 Pa.C.S.A. § 8371.

[8] Because the notice of appeal filed on January 14, 2003 inadvertently omitted Mark and Myrna Mason, a separate notice of appeal was filed on their behalf on January 21, 2003. The two appeals subsequently were consolidated by order of this Court and Appellants have collectively briefed and argued these appeals.

a matter of law, that the ***Michels*** class action settlement was procured by fraud?

3. Did the trial court commit an error of law in holding that a Pennsylvania court may enforce an injunction entered by the court of another state as part of a class action settlement?

(Appellants' Brief at 2.) We first address Appellants' claim that the trial court erred in granting summary judgment to Phoenix by finding, as a matter of law, that the class action notice was adequate.

¶ 13 Our standard of review of an order granting or denying a motion for summary judgment is well established:

> We view the record in the light most favorable to the non-moving party, and all doubts as to the existence of a genuine issue of material fact must be resolved against the moving party. Only where there is no genuine issue as to any material fact and it is clear that the moving party is entitled to a judgment as a matter of law will summary judgment be entered. Our scope of review of a trial court's order granting or denying summary judgment is plenary, and our standard of review is clear: the trial court's order will be reversed only where it is established that the court committed an error of law or abused its discretion.

***Pappas v. Asbel,*** 564 Pa. 407, 418, 768 A.2d 1089, 1095 (2001) (citations omitted).

¶ 14 The doctrine of *res judicata,* which underlies Phoenix's motion for summary judgment, bars repetitious litigation of the same cause of action. ***Dempsey v. Cessna Aircraft Co.,*** 439 Pa. Super. 172, 176, 653 A.2d 679, 681

(1995) (*en banc*). As we have stated, application of this doctrine requires that the lawsuits possess the following common elements: "(1) identity of the thing sued upon; (2) identity of the cause of action; (3) identity of the parties; and (4) identity of the capacity of the parties." ***Taylor v. Shiley, Inc.,*** 714 A.2d 1064, 1066 (Pa. Super. 1998). Ordinarily, a judgment in a properly entertained class action is binding on all class members in any subsequent litigation, and class members who elect not to opt out of a class action are considered full members who must abide by the final judgment, whether favorable or adverse. ***Id.*** As the United States Supreme Court has recognized, however, such a judgment will not be binding on a class member where notice of the class action settlement was inadequate. ***See Phillips Petroleum Co. v. Shutts,*** 472 U.S. 797, 811-812 (1985). In the absence of adequate notice, a class action settlement cannot fix the rights of class members who do not opt out, and cannot bar them from seeking further relief. ***Id.*** Accordingly, as Phoenix concedes, absent class members such as the Masons and the Trustees may collaterally attack the ***Michels*** class action settlement on the ground that they did not receive adequate notice of the settlement. ***See Twigg v. Sears Roebuck & Co.,*** 153 F.3d 1222, 1226 (11th Cir. 1998).

¶ 15 Adequate notice of a class action settlement is required by the constitutional mandate of due process. ***Id.*** This fundamental principle was first set forth in ***Mullane v. Central Hanover Bank & Trust Co.,*** 339 U.S. 306 (1950):

> An elementary and fundamental requirement of due process in any proceeding which is to be accorded finality is notice reasonably calculated, under all the circumstances, to apprise interested

> parties of the pendency of the action and afford them an opportunity to present their objections. The notice must be of such nature as reasonably to convey the required information, and it must afford a reasonable time for those interested to make their appearances. But if with due regard for the practicalities and peculiarities of the case these conditions are reasonably met the constitutional requirements are satisfied. . . . But when notice is a person's due, process which is a mere gesture is not due process.

***Id.*** at 314-315 (citations omitted). Notice is, as the Pennsylvania Supreme Court has stated, "the most basic requirement of due process." ***Pennsylvania Coal Mining Ass'n v. Insurance Dept. of Pa.,*** 471 Pa. 437, 452, 370 A.2d 685, 692 (1977).

¶ 16 To satisfy due process, notice of a class action settlement must be "reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections." ***Mullane,*** 339 U.S. at 314. Although the notice need not be entirely comprehensive, the notice must not be misleading or materially incomplete. ***Weinberger v. Kendrick,*** 698 F.2d 61, 70 (2d Cir. 1982). The notice must contain an adequate description of the proceedings written in objective, neutral terms that may be understood by the average absentee class member. ***In Re Nissan Motor Corp. Antitrust Litig.,*** 552 F.2d 1088, 1104 (5th Cir. 1977). The notice also must "contain information that a reasonable person would consider to be material in making an informed, intelligent decision of

whether to opt out or remain a member of the class and be bound by the final judgment." ***Id.*** at 1105.[9]

¶ 17 The question of whether constitutionally adequate notice can be provided to claimants whose injuries have not manifested at the time of the settlement is particularly problematic, and one which requires close scrutiny in light of the Supreme Court's decision in ***Amchem Products, Inc. v. Windsor,*** 521 U.S. 591 (1997). In ***Amchem,*** the Supreme Court confronted a challenge to class certification for settlement purposes in an asbestos litigation. The class defined in the complaint included both individuals who were presently injured, as well as individuals who had only been exposed to asbestos and had not yet manifested any injury. ***Id.*** at 602. The Court held that this "sprawling" class was improperly certified because the class in that case could not satisfy the requirements of common issue predominance and adequacy of representation. ***Id.*** at 628.[10] Although the Court did not rule on the issue of whether the notice given in that case was adequate, the

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[9] As some courts have recognized, an adequate notice also should contain information about either the amount or range of recovery. ***See, e.g., Missouri v. Chadwick,*** 956 S.W.2d 369, 386 (Mo. Ct. App. 1997) (notice was inadequate as it failed to estimate the number of persons in the class, the total potential number of claims, the number of claims which it was estimated would be filed, the formula for determining each class member's recovery, or any other information by which the absent class members could determine their potential amount or range of recovery).

[10] As to the adequacy-of-representation requirement of Rule 23(a)(4) of the Federal Rules of Civil Procedure, which governs class actions, the Court noted that the interest of present claimants asserting asbestos-related injuries conflicted with the interests of future claimants, both those who knew they had been exposed but had not manifested any injury, and those who had no manifest injury and did not even know that they had been exposed. ***Amchem,*** 521 U.S. at 622-25.

Court questioned whether constitutionally adequate notice could ever be given to exposure-only claimants, particularly those who might not know that they had been exposed to asbestos dust or injured by it. The Court pointed out "the gravity of the question whether class action notice sufficient under the Constitution and Rule 23 could ever be given to legions so unselfconscious and amorphous." ***Id.***

¶ 18 In granting Phoenix's motion for summary judgment, the trial court in this case concluded that the ***Michels*** class action notice was constitutionally adequate because, in its opinion, "[t]here could be no doubt that both the Notice of Settlement and Phoenix's Brochure clearly conveyed to the reader that a policy such as the one at issue was covered by the class action settlement." (Trial Court Opinion, 2/14/03, at 7.) The trial court further held that it was unreasonable as a matter of law for the Trustees and the Masons to rely on any representations of Phoenix or its agent, Lenenberg, that were contrary to or inconsistent with the notice and settlement package. (***Id.*** at 8.) According to the trial court,

> "[s]ince Phoenix was the opponent in the *Michels* lawsuit which Plaintiffs joined, they cannot be heard to say that it was *reasonable* to rely upon representations of Phoenix or the man they say they believed was its agent regarding the effect of the settlement. This is a matter about which reasonable minds could not differ. You do not consult your enemy about how to interpret documents in dispute.

(Trial Court Opinion, 12/23/02, at 1-2.)

¶ 19 Appellants argue that the trial court erred in granting summary judgment on the notice issue because there was at least a question of fact regarding the adequacy of

the notice, and it was not unreasonable as a matter of law for them to rely on Phoenix's representations under the circumstances, where they had an ongoing business relationship with Phoenix relating to the policy, Phoenix was the only source of information concerning their policy, and Phoenix was specifically obligated to provide information about the class action by the terms of the settlement. For the following reasons, we agree.

¶ 20 As Appellants point out, nothing in the class action notice specifically referred to second-to-die policies, or to the possibility that a vanished premium for a second-to-die policy including an Optionterm component could reappear and quickly escalate. Neither did anything in the notice disclose that after the two years of Optionterm Charge Offset had been funded by Phoenix, policyholders such as Appellants with a second-to-die policy could have to pay millions of dollars of out-of-pocket payments to maintain sufficient Optionterm coverage to meet a target amount of insurance projected, sold, and repeatedly illustrated even during the opt-out phase of the class action as requiring no out-of-pocket payment whatsoever.

¶ 21 Significantly, Phoenix's own corporate designee, Robert Lautensack, admitted in his deposition that nothing in the class action notice provided specific information to enable the Masons and the Trustees to make an informed decision with respect to claims concerning out-of-pocket premiums required after the death of the first insured:

> Q. I've already asked you this but I want to be sure it is covered, because it is one of the specific items in the corporate notice.

> You indicated that there's no specific information within the class action notice to enable the plaintiffs – to make the Masons and trustees to make an informed decision with respect to claims concerning out-of-pocket premium payments required after the death of the first insured under the policy, is that correct?
>
> A. That is correct.

(Deposition of Robert Lautensack, 10/30/01, at 189-90 (Exhibit F to Memorandum In Support of Plaintiffs' Motion for Summary Judgment, Vol. I) (R.R. 697a).) Paul Michael Fischer, Phoenix's Vice President of Life and Annuity, similarly testified that he did not recall the issue of out-of-pocket premiums due upon the death of the first insured being part of the settlement. (Deposition of Paul Michael Fischer, 6/28/02, at 219 (Exhibit D to Memorandum In Support of Plaintiffs' Motion for Summary Judgment, Vol. I) (R.R. 560a).)

¶ 22 Appellants in this case appear to have been in a situation analogous to many of the exposure-only claimants in ***Amchem, supra.*** At the time of the settlement, Appellants had no reason to believe they had or were being defrauded as they had received numerous assurances from Phoenix and Lenenberg that their policy coverage was as originally represented in 1989. They arguably did not, as they claim, have the information or foresight needed to decide, intelligently, whether to stay in or opt out of the class action. Neither could Appellants have invoked the ADR process because, as Phoenix does not dispute, ADR was only available to those who had evidence of misrepresentation. Appellants did not know anything was wrong with their policy, or have any reason

to doubt the veracity of Phoenix's and Lenenberg's representations, until over a year after the period for invoking ADR ended. Under these ci :umstances, we find that the trial court erred in concluding that the class action notice was constitutionally adequate as a matter of law.[11]

¶ 23 Neither can we agree with the trial court that it was unreasonable as a matter of law for Appellants to rely on Phoenix's representations about their policy, or on the purported advice of Lenenberg in telling them they should not opt-out or invoke ADR. As stated above, Phoenix was not just a defendant. Under the terms of the class action settlement, Phoenix was obligated to provide a hotline to answer questions.[12] Further, Phoenix was continuing to

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[11] Moreover, there is some support for the proposition that a party to a class release is precluded from interposing the release as a defense if it has failed to provide information to enable the class members to claim benefits under the class action settlement. ***See In re Holocaust Victim Assets Litigation,*** 105 F. Supp. 2d 139, 158 (E.D.N.Y. 2000) (court concluded that certain banks could not avail themselves of the benefits of releases under the settlement agreement while continuing to conceal from the class information needed to take advantage of the benefits conferred by the settlement agreement). In this case, Phoenix arguably is precluded from raising the ***Michels*** class action settlement as a bar to Appellants' claims if, as Appellants' allege, Phoenix concealed from Appellants information needed to apprise them that the ADR process was a relevant consideration (i.e., that Phoenix had misrepresented their policy terms).

[12] Moreover, by the express terms of the settlement agreement, agents such as Lenenberg were permitted to discuss the proposed settlement with Phoenix policy owners. (Stipulation of Settlement, 8/5/96, at 57.) As Dona D. Young, now Phoenix's Chairman of the Board, President and Chief Executive Officer, observed at the time in an internal videotape for Phoenix's agents, "[t]he most natural thing in the world for a policyholder to do is to call their agent and ask for the agent's advice." (Transcript of Phoenix videotape entitled "Michel's Lawsuit Video Conference Settlement Class Action Lawsuit," 8/12/96, at 40 (R.R. at 1606a).) Indeed, Phoenix promoted the settlement to its

(Continued on following page)

service the policy in the normal course,[13] so that the allegedly incomplete and misleading information it provided arguably came from it in its status as Appellants' continuing insurer, and not as part of the adversary process. Phoenix was the exclusive source of information concerning the projected performance of the policy.

¶ 24 We further note that Lenenberg's alleged advice to Appellants that their policy was not affected by the proposed settlement and that they should not opt out, if given, likely prevented Appellants from making a free and unfettered decision to opt out of the class. ***See Georgine v. Amchem Products, Inc.,*** 160 F.R.D. 478, 497 (E.D. Pa. 1995) (court ordered second notice and opt-out period because, even though notice was adequate, communications by counsel opposed to the settlement likely confused and misled class members, prohibiting them from making a "free and unfettered" decision to opt out of the class).

¶ 25 For all of the foregoing reasons, we find that the trial court erred in granting Phoenix's motion for summary judgment because a question of fact existed as to whether, under all the circumstances of this case, the notice given to Appellants was constitutionally adequate. Accordingly, we reverse the order entering summary judgment.

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various agents as providing an opportunity for these agents to sell more insurance to class members and to market themselves and Phoenix to customers they might not have seen in a long time.

[13] As the January 7, 1997 letter from Phoenix's then President and Chief Executive Officer reflects, agents were to continue conducting "business as usual" with their policyholders during the settlement period. (Phoenix letter from Robert Fiondella to producers, 1/7/97 (Exhibit 41 to Memorandum In Support of Plaintiff's Motion for Summary Judgment, Vol. 4) (R.R. 1802a).)

¶ 26 Appellants next argue that the trial court erred in granting summary judgment in favor of Phoenix on the alternative basis that the ***Michels*** class action settlement was entitled to full faith and credit because Appellants could not show as a matter of law that it was procured by fraud. It appears that the sole basis for the trial court's ruling in this regard was the court's determination that it was unreasonable as a matter of law for Appellants to rely on the representations of Phoenix and Lenenberg, whether fraudulent or not. On remand, we direct the trial court to reconsider this aspect of Phoenix's summary judgment motion in light of this opinion.[14]

¶ 27 Order entering judgment **REVERSED**. Case **REMANDED**. Jurisdiction **RELINQUISHED**.

Judgment Entered:

/s/ Eleanor R. Valecko
Deputy Prothonotary

DATE: May 26, 2004

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[14] Given our resolution of this appeal, we do not reach Appellants' third issue on appeal.

IN THE COURT OF COMMON PLEAS OF
ALLEGHENY COUNTY, PENNSYLVANIA

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| ANDREA D. WILKES, DAVID H. EHRENWERTH and CHARLES K. CLARK, as Trustees of the Mark E. and Myrna L. Mason Irrevocable Trust, MARK E. MASON, and MYRNA L. MASON.<br><br>Plaintiffs,<br><br>vs.<br><br>PHOENIX HOME LIFE MUTUAL INSURANCE COMPANY, a corporation, and BALANCED EQUITIES, INC., a corporation,<br><br>Defendants. | ) CIVIL DIVISION<br>) GD 00-745<br>)<br>) **OPINION**<br>) Filed by the Honorable<br>) JUDITH L. A. FRIEDMAN<br>)<br>) Copies mailed to:<br>) David L. McClenahan, Esq.<br>) Joseph Leibowicz, Esq.<br>) Kirkpatrick & Lockhart, LLP<br>) Henry W. Oliver Building<br>) 535 Smithfield Street<br>) Pittsburgh, PA 15222<br>)<br>) Jeffrey G. Weil, Esq.<br>) George M. Gowen, III, Esq.<br>) Dechert Price & Rhoads<br>) 1717 Arch Street<br>) Philadelphia, PA 19103-2793<br>)<br>) John P. Edgar, Esq.<br>) Sherrard, German &<br>) Kelly, PC<br>) 35th Floor, One Oliver Plaza<br>) Pittsburgh, PA 15222-2602 |

## OPINION

### INTRODUCTION

Plaintiffs have appealed from this Court's order of December 23, 2002 granting summary judgment in favor of Defendant Phoenix Home Life Mutual Insurance Company (hereinafter, "Phoenix"). As noted in the Memorandum in Support of the order, the basis for granting

summary judgment was not the underlying merits of Plaintiffs' case, about which the Court concluded there were material facts in dispute, but rather the grant was compelled by the doctrine of *res judicata*, which arises from the settlement of the case of *Michels v. Phoenix Home Life Mutual Ins. Co.*, Index No. 5318-95 (N.Y. Sup. Ct. Albany Cty.) (hereinafter, *Michels*), a New York State class action suit.

FACTUAL BACKGROUND

Plaintiffs contend that Phoenix, directly and through its alleged agent Sander Lenenberg (hereinafter, "Agent), misled Plaintiffs from 1989 through 1993, and again in 1994 regarding an estate-planning insurance policy (hereinafter, "the Policy") they had bought to provide liquidity for the estate of the Second to Die (hereinafter, "Estate") of the two spouses (Plaintiffs Mark and Myrna Mason) whose lives were insured under the Policy. Plaintiffs also contend that Phoenix directly and through the Agent misled them about the effect of the *Michels* settlement on them.

The Plaintiffs' greatest concern at the time of purchase of the Policy was that the annual premiums for the Policy would *decrease* as the Masons got older, and that they would "vanish" after 15 years, so that Mrs. Mason, statistically the most likely to be the "Second to Die," would not have the burden of paying large premiums after the death of Mr. Mason in order to keep the Policy in force. The Agent assured them repeatedly that the Policy was suitable for their needs and that the premiums would start off at roughly $80,000, would decrease to roughly $60,000, then to roughly $40,000, and after 2003, would

"vanish" altogether, leaving the Estate with roughly $4 million of whole life proceeds and $3 million of term proceeds, under a rider known as the Option Term Rider. (*See* Plaintiffs' Memorandum in Support of Motion for Summary Judgment, ¶ 33 and 34.)

In 1996 the *Michels* class action notice was received by Plaintiffs. Later in 1996, the consent order was entered and the Settlement Package was also sent to the Plaintiffs who chose to remain in the class. Eventually, after the discovery in 1998 of a separate unrelated crime by the Agent, Plaintiffs investigated the Policy.

As part of their investigation, Plaintiffs asked Phoenix to provide illustrations of what premiums would be required to keep the Policy in force if Mr. Mason were to die at age 83. (Plaintiffs' Memorandum, ¶ 225-227.) Although Phoenix could, and for its own use did, run a "worst case" scenario for the Policy, it did not include that scenario in the information sent to Plaintiffs; instead, it sent them only the same kind of reassuring scenarios that the Agent had provided earlier, indicating that the premium would vanish after 2003. (Plaintiffs' Memorandum, ¶ 201-210.) In other words, there is evidence, albeit disputed, that Phoenix concealed from Plaintiffs, and possibly the Agent, the possibility that if the Second to Die outlived the First to Die by a certain number of years, the supposedly "vanished" premiums would re-surface, in spades. Depending on the number of years the Second to Die survived, the re-surfaced premiums could result in the need to pay $6 million for the $7 million dollars of coverage. This would obviously defeat the purpose of the Policy, which was to *provide* liquidity for the Estate, not drain liquidity away.

Phoenix claimed that Plaintiffs had the information to determine this, but the Court concluded that Phoenix could not avoid liability if it intentionally gave conflicting information, as alleged by Plaintiffs, particularly since the incorrect version was clearly expressed and demonstrated and the truth was hidden and muddled. However, and more importantly, the Court also concluded that Phoenix was entitled to Summary Judgment because of the doctrine of *res judicata*, despite the existence of factual disputes related to the underlying merits of Plaintiffs' claims against them.

ISSUES ON APPEAL

Plaintiffs raise six issues in their Statement of Matters Complained of on Appeal (hereinafter, "Statement"), which are summarized below:

1. That the Court erred when it held as a matter of law on summary judgment that the *Michels* class action notices "clearly cover the type of insurance policy here."

2. That the Court erred when it implicitly held on summary judgment that there was no genuine issue of material fact as to whether the *Michels* class action notice was constitutionally inadequate as to the Masons and the Trustees.

3. That the Court erred when it held on summary judgment that it was unreasonable as a matter of law for the Masons and the Trustees to rely on the representations of Phoenix itself in connection with the status of the Policy and the impact of the *Michels* class action settlement.

4. That the Court erred when it held on summary judgment that it was unreasonable as a matter of law

for the Masons and the Trustees to rely on the representations of Mr. Lenenberg in connection with the status of the Policy as of the time Plaintiffs became aware of the proposed settlement of the class action.

5. That the Court erred when it held as a matter of law on summary judgment that the Masons and the Trustees could not carry their burden of proof that *res judicata* was precluded by Phoenix's fraud on the Masons and Trustees in connection with the *Michels* class action settlement.

6. That the Court erred when it held as a matter of law on summary judgment that the Masons' and the Trustees' claims were barred by the "federal court injunction" where there was no federal court injunction and Phoenix did not seek to enforce the injunction entered by the New York State court in *Michels* in that court, where the New York State court is the only court with jurisdiction to enforce that injunction under both settled legal principles and the terms of the *Michels* final judgment itself.

The Court believes these issues can be condensed into three:

1. Whether the *Michels* class action, of which Plaintiffs undisputedly had actual notice, involved policies such as the Policy purchased by Plaintiffs, so that *res judicata* applies. (Statement, Items 1 and 2.)

2. Whether Plaintiffs were reasonable in relying on the representations of Phoenix or of Lenenberg *with regard to the effect of joining in the class action and the settlement.* (Statement, Items 3, 4 and 5.)

3. Whether the action is also barred by the injunction issued by the New York State Court (inadvertently referred to in the Memorandum in Support of Order as a "federal court" injunction).

DISCUSSION

1. THE *MICHELS* SETTLEMENT INCLUDED THE POLICY PURCHASED BY PLAINTIFFS.

Plaintiffs contend that the Policy was not among the types of insurance covered by the *Michels* Complaint or the Settlement and pointed out that the Complaint in *Michels* (which was a second amended complaint) does not refer explicitly to "Second to Die" policies, which is the type of policy involved in the instant case. The Plaintiffs also pointed to admissions in the depositions of various high level employees of Phoenix that it was Phoenix, and not the class action plaintiffs, who inserted the Option Term Rider into the Settlement. Phoenix, on the other hand, pointed out that "vanishing premiums" were mentioned in the Federal Complaint and that the Option Term type of rider was in any case made part of the Settlement. Phoenix also pointed out that Plaintiffs received an individual mailing of the Notice of the proposed Settlement. Phoenix argued that Plaintiffs therefore had ample opportunity to object or opt out or seek ADR, so that *res judicata* applies to their instant action.

The Notice of Settlement itself fully describes policies such as the one at issue. At page 2 of the Notice of Settlement of August 1996, the "Description of the Lawsuit" is set forth below, with the pertinent parts in bold:

## 2. DESCRIPTION OF THE LAWSUIT

This action consolidates two class action lawsuits against Phoenix. The first action, *William Michels v. Phoenix Home Life Mutual Insurance Company*, was filed in the Supreme Court of the State of New York, County of Albany, on September 22, 1995. The *Michels* complaint was amended on October 27, 1995. The second action, *Jason A. Sokolov v. Phoenix Home Life Mutual Insurance Company*, was filed in the United States District Court for the District of Massachusetts on March 15, 1996. On August 5, 1996, a Joint Motion to Dismiss without Prejudice was filed in the *Sokolov* action, and a consolidated amended complaint was filed in the *Michels* action joining the *Sokolov* and *Michels* claims. The Plaintiffs make allegations concerning (*i*) how Phoenix made use of a method of using dividends to pay premiums on a whole life policy, or interest credited on a universal life policy, rather than paying them in cash, in order that no further out-of-pocket premium would be due after a fixed period of time, which sales concept was variously referred to as "Quick Pay" or "Rapid Pay," as well as Phoenix's use of dividends to help meet the costs of a rider known as Optionterm; (*ii*) the sale of life insurance by portraying it as an investment, savings, retirement or other similar plan without disclosing that it is life insurance or the nature of the policy's benefits; (*iii*) the replacement of any existing life insurance policy with a new life insurance policy, or the sale of a new life insurance policy funded in whole or in part using an existing policy's cash value; and (*iv*) the failure to disclose material information in connection with the introduction of new methods for calculating dividends and crediting rates. The

> allegations in the lawsuits include claims that Phoenix misled policy owners in these and other circumstances.

In addition, the "Question and Answer" brochure which was a part of the "Settlement Package" (Defendant's Appendix of Exhibits to Motion for Summary Judgment on Class Action Defenses, Exhibit "E"), describes one of the claims of the lawsuit as:

> How the company sold vanishing premium policies, which Phoenix called "Quick Pay" or "Rapid Pay" policies. Vanishing premium is a sales concept under which policy values, rather than out-of-pocket payments, are used to pay premiums on whole life policies. For universal life policyholders, a similar concept exists for using interest credited to their policies' cash value to pay policy charges as they come due.

Question and Answer brochure, p. 1.

There can be no doubt that both the Notice of Settlement and Phoenix's Brochure clearly conveyed to the reader that a policy such as the one at issue was covered by the class action settlement. The Court properly concluded that the doctrine of *res judicata* barred the instant action. For the same reasons, the Notice and Settlement Package meet Constitutional requirements.

2. IT WAS UNREASONABLE OF PLAINTIFFS, AS A MATTER OF LAW, TO RELY ON REPRESENTATIONS THAT ARE CONTRARY TO OR INCONSISTENT WITH THE UNAMBIGUOUS CONTENTS OF THE NOTICE AND SETTLEMENT PACKAGE.

This group of items is related to the issue of the constitutionality of the Notice and Settlement Package. Plaintiffs contended that, even if their policy was covered by *Michels*, the Notice of the Settlement as to them specifically was constitutionally deficient so as to permit this Court to consider their instant action despite the *Michels* injunction. The basis for this is an alleged fraud on the New York State Court, on the attorneys for the class, and on the Plaintiffs themselves who were sent, contemporaneously with the settlement notices, the falsely reassuring information about the status of their policy premiums which caused them to believe that they had no basis for seeking one of the forms of relief offered in the Settlement, alternate dispute resolution (hereinafter, "ADR"), and leading them instead to rely on a form of relief from the other major category provided in the Settlement, General Policy Relief, in particular the relief for those policies with an Option Term Rider, which was the eventual payment by Phoenix of two of the first three years worth of premiums due after the death of the First to Die.

Plaintiffs undisputedly received, and are held to have read, the Notice of the proposed settlement of the class action and the Settlement Package. The language of the Notice very clearly includes reference to "claims that Phoenix *misled* policy owners in these and other circumstances." Plaintiffs were on notice by early Fall 1996 that

they might have been misled by Phoenix, and, implicitly, by the Agent. Yet in deciding whether to settle, they relied without question on Phoenix and Mr. Lenenberg to evaluate whether the settlement adequately protected Plaintiffs' interests. There was no *fiduciary* relationship between Phoenix and Plaintiffs, which might justify such blind reliance. In fact, there was an *adversary* relationship: it must be remembered that Plaintiffs voluntarily were among the class plaintiffs in *Michels* where, as here, Phoenix was the Defendant.

To the extent Plaintiffs' attack on the constitutionality of the Notice depends on their having been misled by Phoenix and the Agent, the Court correctly concluded, as a matter of law, that any reliance by Plaintiffs on their representations as to the settlement was unreasonable.

3. AN INJUNCTION ISSUED BY ANOTHER COURT, WHETHER STATE OR FEDERAL, MUST BE GIVEN FULL FAITH AND CREDIT SO LONG AS REQUIRED CONSTITUTIONAL PROTECTIONS WERE PROVIDED IN THE ISSUING COURT.

Again, the Notice to Plaintiffs was clear, the allegations of fraud were not made out by Plaintiffs, and the constitutional protections were met by the New York Court. The injunction is entitled to full faith and credit, although it was not the primary basis for the grant of summary judgment.

CONCLUSION

Summary judgment was properly entered in favor of Phoenix.

[By the Court]

/s/ Friedman, J.

DATED: February 14, 2003

IN THE COURT OF COMMON PLEAS OF
ALLEGHENY COUNTY, PENNSYLVANIA

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| ANDREA D. WILKES, DAVID H. EHRENWERTH and CHARLES K. CLARK, as Trustees of the Mark E. and Myrna L. Mason Irrevocable Trust, MARK E. MASON, and MYRNA L. MASON,<br><br>Plaintiffs,<br><br>vs.<br><br>PHOENIX HOME LIFE MUTUAL INSURANCE COMPANY, a corporation, and BALANCED EQUITIES, INC., a corporation,<br><br>Defendants. | ) CIVIL DIVISION<br>)<br>) GD 00-745<br>)<br>) **MEMORANDUM IN SUPPORT OF ORDER AND ORDER OF COURT**<br>)<br>) Filed by the Honorable JUDITH L. A. FRIEDMAN<br>)<br>) Copies mailed to:<br>)<br>) David L. McClenahan, Esq.<br>) Joseph Leibowicz, Esq.<br>) Kirkpatrick & Lockhart, LLP<br>) Henry W. Oliver Building<br>) 535 Smithfield Street<br>) Pittsburgh, PA 15222<br>)<br>) Jeffrey G. Weil, Esq.<br>) George M. Gowen, III, Esq.<br>) Dechert Price & Rhoads<br>) 1717 Arch Street<br>) Philadelphia, PA 19103-2793<br>)<br>) John P. Edgar, Esq.<br>) Sherrard, German &<br>) Kelly, PC<br>) 35th Floor, One Oliver Plaza<br>) Pittsburgh, PA 15222-2602 |

MEMORANDUM IN SUPPORT OF ORDER

After a review of the Motions for Summary Judgment and the voluminous attachments thereto, the Court has concluded that the *Michels* settlement does bar the instant suit, and that the Motion for Summary Judgment filed by

Phoenix Home Life Mutual Insurance company (hereinafter, "Phoenix") must be granted. The notices sent in connection with that settlement clearly cover the type of insurance policy at issue here. Furthermore, there is no merit to the contention that Plaintiffs *reasonably* relied on the statements of Mr. Lenenberg, who they believe was acting as an agent of Phoenix at the time of the settlement, when he led the Plaintiffs to believe their premiums would nevertheless vanish even though settlement notices clearly state that this failure to vanish was one of the problems asserted in the lawsuit. Since Phoenix was the opponent in the *Michels* lawsuit which Plaintiffs joined, they cannot be heard to say that it was *reasonable* to rely upon representations of Phoenix or the man they say they believed was its agent regarding the effect of the settlement. This is a matter about which reasonable minds could not differ. You do not consult your enemy about how to interpret documents in dispute. The fraud exception cannot, therefore, be met. The matter is *res judicata* and is also barred by the federal injunction.

Were we to reach the underlying merits of the instant action, the case is "ripe" despite Phoenix's claim to the contrary. Plaintiffs have already suffered some harm in the form of premiums being higher than promised. They will soon be confronted with a decision regarding continuing to keep the policy in force now that it is clear that it will not suit their needs. As to the claim that Phoenix is liable for the conduct of Lenenberg, there does seem to be a sufficient basis for the Plaintiffs' belief that many of Lenenberg's representations about the policy, both before and after it was purchased, were apparently made with the authority of Phoenix. Although the law of Pennsylvania strongly favors the defense that a broker is not the

agent of an insurance company, it also recognizes that a person can be the agent of two principals, for different purposes. Furthermore, it is doubtful that insurance companies such as Phoenix would be allowed, in Equity, to have provided misleading information to a broker such as Lenenberg and then be able to wash their hands of responsibility for the consequences of the subsequent communication of that misinformation to the ultimate targets of the information, persons such as the Masons and the Trustees. Were the action not otherwise barred, there would be a factual dispute regarding agency, resolvable only by a factfinder, based on the credibility of the various witnesses, including Mr. Ehrenwerth. Because this is a moot point, it will not be dealt with herein.

See Order filed herewith.

[By the Court]

/s/ Friedman, J.

DATED: December 23, 2002

IN THE COURT OF COMMON PLEAS OF
ALLEGHENY COUNTY, PENNSYLVANIA
CIVIL DIVISION

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| ANDREA D. WILKES, DAVID H. EHRENWERTH and CHARLES K. CLARK, as Trustees of Mark E. and Myrna L. Mason Irrevocable Trust, MARK E. MASON, and MYRNA L. MASON, | ) GD 00-745 |
| Plaintiffs, | |
| vs. | |
| PHOENIX HOME LIFE MUTUAL INSURANCE COMPANY, a corporation, and BALANCED EQUITIES, INC., a corporation, | |
| Defendants. | ) FRIEDMAN, J. |

ORDER OF COURT

AND NOW, to-wit, this 23rd day of December 2002, it is hereby ORDERED that the Motion for Summary Judgment filed by Phoenix Home Life Mutual Insurance Company in the captioned matter is GRANTED for the reasons set forth in the accompanying Memorandum in Support of Order.

[By the Court]

/s/ Friedman, J.